DOCUMENT RESUME

ED 403 808 HE 029 853

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TITLE Accounting for Contributions. Understanding the Requirements of FASB Statement No. 116.
INSTITUTION National Association of Coll. and Univ. Business Officers, Washington, D.C.
PUB DATE 96
NOTE 64p.; Supported by a grant from the Follett College Stores Fund for Financial Management.
AVAILABLE FROM National Association of College and University Business Officers, One Dupont Circle, Washington, DC 20036 ($32.95 members; $47.95 nonmembers).
PUB TYPE Reports - Research/Technical (143)

EDRS PRICE MF01/PC03 Plus Postage.
DESCRIPTORS Accountability; Administrative Policy; College Administration; Compliance (Legal); Disclosure; Donors; *Fund Raising; Higher Education; Recordkeeping; *School Accounting; *Standards
IDENTIFIERS *Financial Accounting Standards Board; Gifts

ABSTRACT

Since the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 116, Accounting for Contributions Received and Contributions Made, in June 1993, guidance has been sought in understanding its impact and implementation. Specific key provisions deal with contributions received and contributions made, expiration of restrictions on contributions received, accounting for collections, and recognition of contributed services. To help institutions implement the new standards, the National Association of College and University Business Officers developed a series of workshops and the information in this manual is derived from those workshops. Section 1 is a summary of the key provisions of FASB Statement No. 116 highlighting the changes from previous practice. Section 2 is a detailed explanation of the statement and effects of implementation presented in question-and-answer format, including critical definitions of significant words and phrases. Where appropriate, suggestions are made to aid in implementing the standard. Section 3 is a self study containing specific examples of situations that institutions may encounter in implementation of FASB Statement No. 116. A separate glossary of terms is provided. (Author/JLS)

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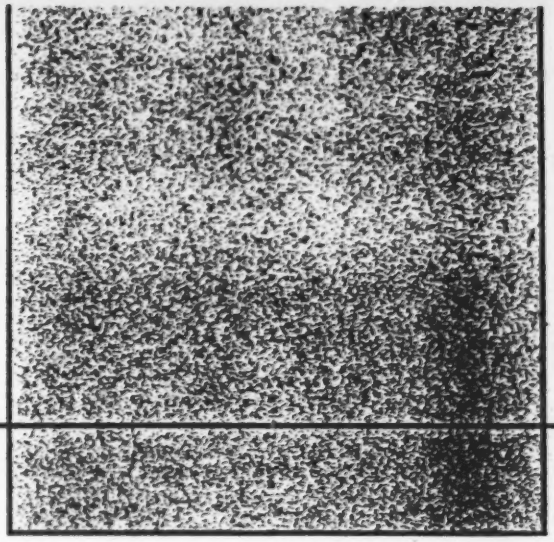

ACCOUNTING FOR CONTRIBUTIONS

Understanding the Requirements of FASB Statement No. 116

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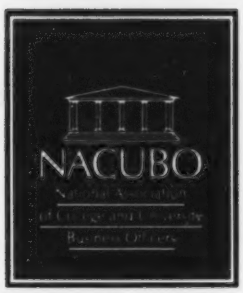
Accounting for Contributions

Understanding the Requirements of FASB Statement No. 116

John S. Ostrom



National Association of College and University Business Officers

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Library of Congress Cataloging-in-Publication Data

Ostrom, John S.
Accounting for contributions : understanding the requirements of FASB Statement No. 116 / John S. Ostrom.
p. cm.
Includes bibliographical references and index.
ISBN 1-56972-003-7
1. Nonprofit organizations—Accounting—Standards—United States. 2. Financial statements—Standards—United States. I. Title.
HF5686.N56088 1996 96-3020
657'.98—dc20 CIP

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National Association of
College and University Business Officers
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Washington, DC 20036

Edited by Anne Kendrick
Designed by Stacey Trey

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Introduction

Since the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 116, *Accounting for Contributions Received and Contributions Made* (FASB Statement No. 116), in June 1993, those affected by the standard have sought guidance in understanding its impact and determining how it should be implemented. Because implementation of the standard requires close cooperation between institutions' business and development offices, staff from these areas have been the most frequent seekers of help. In response to this demand, the National Association of College and University Business Officers (NACUBO) offered a pledge accounting workshop in three different locations in May, November, and December 1995. The information presented in this manual is derived from those workshops.

The workshop program was run as a forum with four faculty members (a business officer, two development officers, and an independent auditor) and presented in a question-and-answer format. Because this approach proved to be highly effective in the workshops, the information contained in this book is presented in the same format.

Two publications are the primary sources of the questions and answers appearing in this manual: *Financial Reporting and Contributions: Guidance for Implementation of FASB Nos. 116 and 117*, a monograph published by Coopers & Lybrand L.L.P. in April 1995, and *The Impact of FASB Standards 116 & 117 on Development Operations: An Overview With Questions and Answers*, a collaborative project produced in 1995 by the Council for Advancement and Support of Education (CASE) and NACUBO. Most of the material contained in these two documents reflects questions asked at a variety of public forums held across the country to address the impact of the changing standards. Other sources of information for this manual include *Accounting and Reporting by Not-for-Profit Organizations: A Comprehensive View of Statements 116 and 117*, a training manual produced by FASB; an exposure draft (ED) issued by the American Institute of Certified Public Accounts (AICPA) on its proposed audit guide for nonprofit organizations; and FASB's December 1995 ED, *Transfers of Assets in Which a Not-for-Profit Organization Acts as an Agent, Trustee, or Intermediary.*

NACUBO is indebted to Coopers & Lybrand L.L.P., CASE, AICPA, and FASB for their permission to use the above-referenced materials in this manual.

Section I of *Accounting for Contributions* is a summary of the key provisions of FASB Statement No. 116 highlighting the changes from current practice. Section II—the largest section of the book—is a detailed explanation of the statement and effects of implementation presented in question-and-answer format, including critical definitions of significant words and phrases. Where appropriate, suggestions are made to aid in implementing the standard. Section III is a self study containing specific examples of situations that institutions may encounter in implementing FASB Statement No. 116.

I. Summary of Key Provisions of FASB Statement No. 116

FASB Statement of Financial Accounting Standards No. 116, *Accounting for Contributions Received and Contributions Made*, establishes standards of accounting and reporting for the following areas:

1. ***Contributions received and contributions made.*** FASB Statement No. 116 applies to all entities—both nonprofit organizations (NPOs), which are generally recipients, and for-profit organizations, which are generally donors. FASB created Statement No. 116 to increase understandability of the financial statements by requiring that common transactions be reported similarly for all entities.
2. ***Expiration of restrictions on contributions received.*** FASB Statement No. 116 establishes a standard for recognizing when donor-imposed restrictions on use of moneys are lifted and money can therefore be reported as "used." The intent is to limit the ability of the institution to pick and choose when restricted funds are "used," an issue that has been a major bone of contention between auditors and institutional management.
3. ***Accounting for collections.*** While not usually a significant issue with colleges and universities, accounting for collections (i.e., works of art and historical treasures) was a major problem for FASB in developing the standard because of the overwhelming opposition by the leadership of museums across the country. The final standard is a clear compromise to overcome that opposition.
4. ***Recognition of contributed services.*** Common practice in higher education has been to ignore most contributed services, but this was a problem area for many other nonprofits, particularly those that relied heavily on volunteers and wished to include the value of the services provided by the volunteers as a revenue source. This practice—used primarily as a means of increasing the percentage applicable to a program and conversely diminishing the percentage of total revenues allocated to administration and fund-raising—is addressed in FASB Statement No. 116.

FASB Statement No. 116 defines

- contributions,
- promises to give,
- donor-imposed conditions, and
- donor-imposed restrictions,

and distinguishes contributions as having

- permanent restrictions,
- temporary restrictions, or
- no restrictions (unrestricted)

as defined by donor.

The statement also classifies time as a restriction, not a condition. Thus, an unconditional promise to give in the future for unrestricted purposes is treated as restricted support. Accordingly, a gift may be unrestricted as to how it may be used (purpose) but restricted as to time (funds not to be received until some time in future), or it may have both purpose and time restrictions.

In the chart below, every item but the last would be recorded as a restricted gift under FASB Statement No. 116:

	PURPOSE	TIME
Future gift for specific purpose	Restricted	Restricted
Future gift for any purpose	Unrestricted	Restricted
Current gift for specific purpose	Restricted	Unrestricted
Current gift for any purpose	Unrestricted	Unrestricted

The NACUBO Accounting Principles Committee argued, unsuccessfully, that time should be considered a condition. However, this would have meant that future gifts/pledges would not be recorded, a conclusion opposite to what FASB sought.

Key Changes from Current Standards

For colleges and universities, the most significant reporting changes resulting from FASB Statement No. 116 are listed below. Statement 116:

- Requires that unconditional promises to give at a future date be reported as contribution revenue in the period the promise is made, provided sufficient evidence of the promise exists in the form of verifiable documentation. Colleges and universities previously excluded such promises from financial reporting.
- Establishes standard for valuing unconditional promises at fair value discounted to the present value of estimated cash flow using a discount rate commensurate with risk. Although not specifically mentioned, this would include split interest, or life income, agreements.
- Requires disclosure of amount of unconditional promises receivable in less than one year, one to five years, and over five years, plus the amount of the allowance for uncollectible promises.
- Defines conditional promises as those that depend upon the occurrence of a specified future uncertain event, requires that they be disclosed as to amounts for each group with similar characteristics.
- Requires a conditional promise to be recognized at the time when the conditions are substantially met.
- Defines inclusion or exclusion of collections—an area that had previously been vague.
- Settles issues of recording and recognizing contributed services. Under Statement 116, contributed services are only recorded if they meet all of the following conditions: (a) create or enhance nonfinancial assets, (b) require specialized skills, (c) need to be purchased if not provided by donation, and (d) are provided by individuals possessing the requisite skills.

- Eliminates institutions' ability to decide when restricted resources are accounted for as spent.
- Treats time as a restriction, not a condition, so that contributions may be for a specific purpose, a specific time, or both.
- Introduces new categories of assets: permanently restricted, temporarily restricted, and unrestricted.

FASB pronouncements provide flexibility in application, and will always be subject to interpretation. Readers and interpreters come from many backgrounds—auditor, financial officer, development administrator, attorney—and each may view the pronouncements in slightly different ways. Further, Statement 116 is intended to apply to all nonprofits, not simply higher education. Rules created for such a diverse universe—one that includes the United Way, Boy Scouts, American Heart Association, churches, museums, libraries, as well as schools and colleges—may not be a perfect fit for every member of the group. While some of these NPOs had good reasons for choosing not to record pledges previously, FASB has concluded that they are not compelling enough to justify permitting differences between the various NPOs to continue.

II. Questions and Answers

This section of *Accounting for Contributions* explores the key areas of concern that commonly arise during the implementation of FASB Statement No. 116. The material is presented in a question-and-answer format and divided into eight categories: (1) applicability of the standard, (2) contributions versus exchanges, (3) conditional contributions, (4) restricted contributions, (5) measuring and accounting for promises to give, (6) other kinds of gifts, (7) other considerations, and (8) recommendations.

1. Applicability of FASB Statement No. 116

Implementation

Question: Why did FASB issue Statement No. 116?

Answer: FASB found considerable inconsistencies in accounting between different types of NPOs, due in part to differences in the various audit guides issued at different times by the AICPA . None of the NPOs will have to change all of their accounting practices because the board's conclusions on any single point are similar to existing guidance in at least one of the four different nonprofit audit guides. In 1986, FASB added a project to its agenda to eliminate these differences, starting with the treatment of depreciation, resolved by the issuance in 1987 of FASB Statement No. 93, which mandates that NPOs must record depreciation on long-lived assets. The next areas to be covered were financial reporting and contributions, which will be resolved by FASB Statement Nos. 116 and 117, both issued in 1993. In November 1995, FASB issued Statement No. 124, *Accounting for Certain Investments Held by Not-for-Profit Organizations.* Finally, an exposure draft on consolidations was also released in the fall of 1995.

FASB believes the result of application of these standards will be an increase in comparability, consistency, and therefore credibility of financial reporting for NPOs. Further, it will put all nonprofits on the same footing.

A. Contributions Received and Made

(i) Colleges and Universities

Question: Does Statement No. 116 change the guidance for public (governmental) colleges and universities?

Answer: Statement No. 116 does not apply to public colleges and universities.

Impact on fund-raising

Question: Because of the state of the economy, many would-be donors are hesitant to make promises out of fear that they may not be able to fulfill the promise when it is due. In such instances, won't FASB's requirements to record promises on the institution's financial records have a negative impact on fund-raising at private institutions? And won't these requirements put independent institutions at a disadvantage with public institutions whose financial accounting falls under GASB regulations that don't require pledge recording?

Answer: The new FASB requirements are unlikely to have any impact on fund-raising. The new requirements simply state that unconditional promises now must be reported as assets on the balance sheet and as restricted revenues in the statement of activities. The standards do not require disclosure of the names or amounts of individual promises, and thus should have no impact on individuals who are contemplating a pledge.

(ii) Voluntary Health and Welfare Organizations

Existing accounting standards for voluntary health and welfare organizations already required the recording of pledges. In fact, colleges and universities were one of the few types of non-profit institutions where current standards permitted but did not mandate recognition and recording of pledges.

(iii) Foundations

Application to public institutions

Question: Private institutions and institutionally related foundations at public institutions are subject to FASB, while public institutions are subject to GASB. Won't this create serious problems for public institutions that have institutionally related foundations?

Answer: Private foundations will be required to follow FASB standards in preparing their individual financial statements. GASB Statement No. 14 permits, with the concurrence of the public institution's auditors, the discrete presentation or blended presentation of a related foundation's financial statements, following FASB standards, with the financial statements of its related public institution.

Fund-raising by foundations

Question: How should foundations reflect the amounts raised for others?

Answer: Amounts received as part of a foundation's fund-raising effort should be evaluated to determine if the assets received should be reflected as contributions. The level of discretion available to the organization determines whether the assets received should be reflected as contributions or as agency transactions. Amounts raised on behalf of others and amounts designated for specific beneficiaries should not be reflected as contributions because either they are agency transactions or the organization is acting as an intermediary. Assets received by foundations that have not been designated by donors for specific beneficiaries may be reported as contributions, depending on the relationship between the foundation and the recipients. In cases where the sole purpose for the existence of the foundation is to raise funds for a specific college or university, all receipts should be recognized as agency transactions.

The issue of whether an organization is acting as an agent is discussed further in part 2 of this section, "Contributions Versus Exchanges."

Question: Who benefits from the recording of gifts through a foundation as an agency?

Answer: Presumably this benefits all users and reviewers of the financial statements of the organization that will ultimately receive the gifts. At present, the assets and revenues of that organization are understated by the amount of gifts that have been given to the foundation but have not yet been forwarded to the final beneficiary.

The proposed interpretation concerning transfers involving agents, trustees, and intermediaries issued by FASB in the December 1995 proposed AICPA audit guide does provide suggested reporting mechanisms that would permit the foundation to reflect the total amount it raised in its financial statements. Such an amount would then be reduced by the amount raised on behalf of others to determine the portion of the total that met the definition of "contributions," that is, the amount over which the foundation had discretion to decide how and by whom it was to be used.

(iv) All Nonprofit Organizations

Applicability to healthcare

Question: Our university has a hospital. Does FASB Statement No. 116 apply to healthcare providers?

Answer: Yes. The AICPA accounting and audit guide, *Audits of Providers of Health Care Services*, is being updated by the AICPA's healthcare committee to incorporate the required changes for Statement 116.

Timing of implementation

Question: When does Statement 116 take effect?

Answer: For institutions with $5 million in total assets, the statement is effective for fiscal years beginning after December 15, 1994. For institutions operating on a June 30 fiscal year, the new standards would first be effective for fiscal year 1995-96. For those with less than $5 million in total assets, they would be effective for fiscal year 1996-97.

(v) For-Profit Organizations

Impact on donors

Question: Does this standard have any impact on for-profit organizations, like corporations, that are frequently substantial donors?

Answer: Yes. The standard addresses both sides of the gift transaction. Just as the institution receiving the gift must recognize a pledge, so must the donor reflect the making of the gift. If a donor makes a multiyear commitment, it must record the present value of the future payments as a liability in the year when the commitment is made.

Donors and multiyear pledges

Question: Won't this tend to make donors reluctant to make multiple year commitments?

Answer: Although some observers may disagree, the standard is unlikely to have any

major impact on fund-raising. Foundations, corporations, and other major donors are not likely to change their giving patterns because of a change in accounting standards. What may happen is that some multiyear promises will be written with sufficient escape clauses to make them conditional and therefore not recordable, but the corporations will continue to follow their normal practice in honoring the intent.

2. Contributions Versus Exchanges

Defining contributions and exchange transactions

Question: What is the difference between a contribution and an exchange?

Answer: FASB Statement No. 116 defines a contribution as "an unconditional transfer of cash or other assets to an entity, or a settlement or cancellation of its liabilities in a voluntary nonreciprocal transfer by another entity acting other than as an owner." The key words are *unconditional, voluntary, nonreciprocal,* and *nonowner.*

An exchange transaction is a reciprocal transfer in which each party receives and sacrifices something of approximately equal value. The purchase of goods and services, the sale of merchandise from a store, or the rendering of a service for a fee are examples of exchange transactions.

A. Characteristics of a Contribution

Contributions have four characteristics that distinguish them from other types of transactions. A contribution is

- a nonreciprocal transfer (the donor receives nothing in exchange for the donation, or receives something of substantially less value than the gift given),
- made or received voluntarily (there is no compulsion for the donor to make the gift)
- a transfer to or from non-owners (the transaction is not an investment; the donor has no ownership in the recipient organization), and
- unconditional (no hurdles or barriers must be overcome in receiving the gift although specific instructions or restrictions may exist on how the funds are to be used).

B. Characteristics of an Exchange

An exchange has two distinguishing features. An exchange is

- a reciprocal transfer (the donor receives something in exchange for the donation), and
- a transfer in which both parties receive and sacrifice equal values (if the exchange is unequal, it may be part contribution and part exchange).

Figure 1

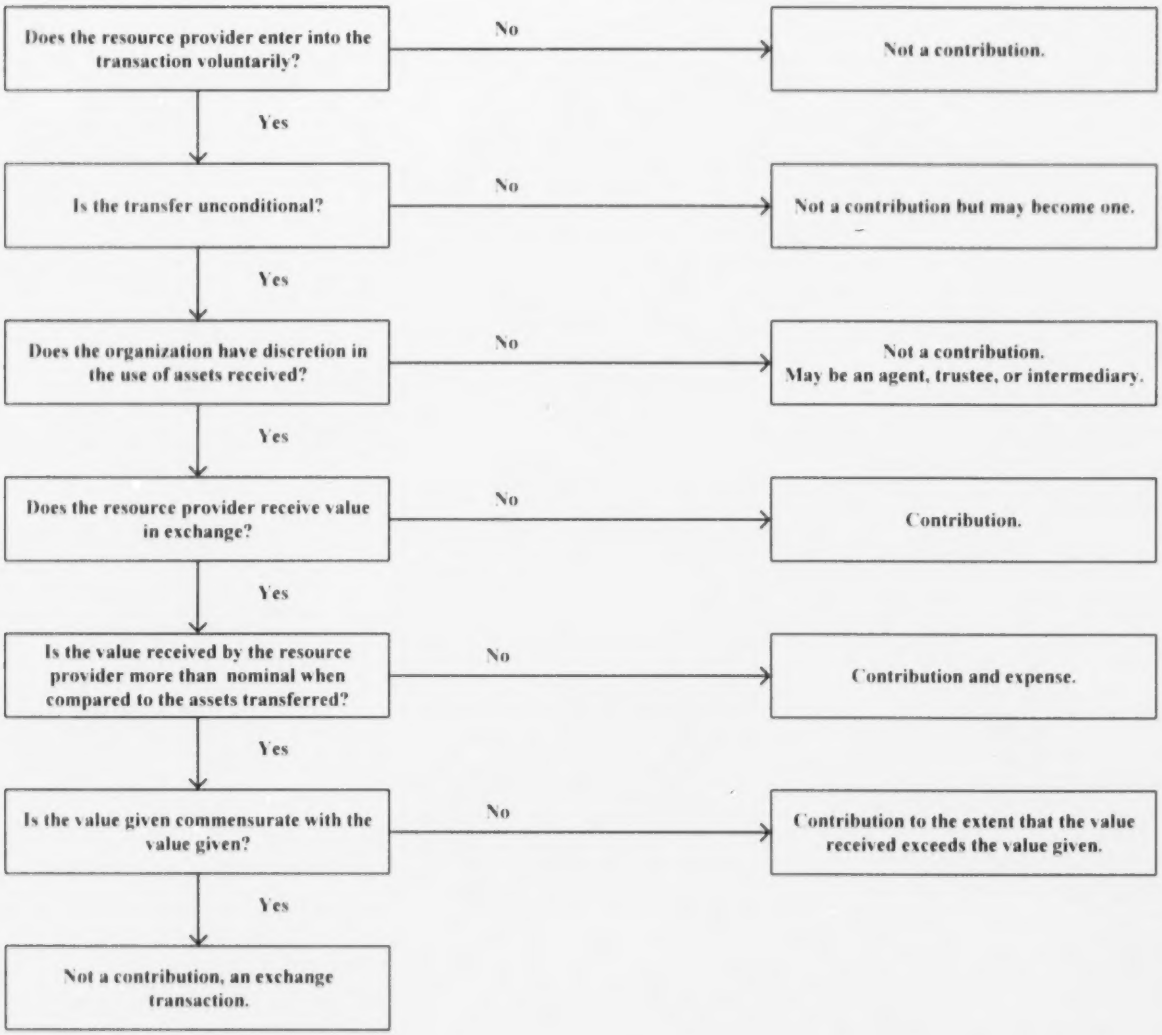
Indicators Useful in Distinguishing Contributions from Exchange Transactions

The indicators below provide guidance on how to classify transactions. Depending on the facts and circumstances, some indicators may be more significant than others; however, no single indicator is determinative of a particular transaction's classification.

Indicator	Contribution	Exchange
Recipient NPO's intent in soliciting the asset	Recipient NPO solicits the asset as a contribution	Recipient NPO seeks resources in exchange for specified benefits
Resource provider's intent for the asset to be provided	Resource provider asserts that it is making a donation to support NPO's programs	Resource provider asserts that it is transferring resources in exchange for specified benefits
Method of delivery	The method of delivery of the asset to be provided by the recipient NPO is at the discretion of the NPO	The method of delivery of the asset to be provided by the recipient NPO is specified by the resource provider
Method of determining payment	Payment is a subsidy to the recipient NPO's cost of providing the asset; the total payment is based on a budget request rather than on specific criteria	Payment is the recipient NPO's cost of providing the asset, or the cost plus a markup; the total is based on the quantity of assets delivered
Penalties assessed if NPO fails to make timely delivery of assets	Penalties are limited to the delivery of assets already produced and the return of the unspent amount (the NPO is not penalized for nonperformance)	Provision for economic penalties exists beyond the amount of the payment (the NPO is penalized for nonpayment)
Delivery of assets to be provided by the recipient NPO	Assets are to be delivered to individuals or organizations other than the provider	Assets are to be delivered to the resource provider or to individuals or organizations closely connected to the resource provider

Figure 2

Identifying a Contribution Transaction


Does the resource provider enter into the transaction voluntarily?
No
Not a contribution.
Yes
Is the transfer unconditional?
No
Not a contribution but may become one.
Yes
Does the organization have discretion in the use of assets received?
No
Not a contribution.
May be an agent, trustee, or intermediary.
Yes
Does the resource provider receive value in exchange?
No
Contribution.
Yes
Is the value received by the resource provider more than nominal when compared to the assets transferred?
No
Contribution and expense.
Yes
Is the value given commensurate with the value given?
No
Contribution to the extent that the value received exceeds the value given.
Yes
Not a contribution, an exchange transaction.

Assumption: The transaction is not a tax incentive, tax exemption, or tax abatement. The resource provider is not acting as an owner of the recipient organization.

C. Other Considerations

(i) Agency Transactions

Intermediary-agent transactions

Question: How does an organization determine whether it is acting as an intermediary or an agent in a transaction?

Answer: In December 1995, FASB issued an exposure draft titled *Transfers of Assets in Which the Not-for-Profit Organization Acts as an Agent, Trustee, or Intermediary,* which speaks very specifically to this issue. FASB makes it clear that an intermediary, as described in Statement 116, is to be narrowly defined as a "facilitator" between a potential donor and a potential donee, but is neither a donor nor a donee itself. In contrast, an agent is defined as one who acts on behalf of a principal, which may be either a resource provider (donor) or a beneficiary (donee), but has no discretion on when or to whom the gift is given. A fund-raising organization, such as the United Way, that solicits contributions designated for a specific agency—such as the Boy Scouts or the Red Cross—and then allocates the funds raised to those various purposes, would be an example of an agent for a resource provider, assuming the resource provider does not specify the beneficiary. A foundation that raises moneys on behalf of a specific charity would be an agent for a beneficiary.

In the "Proposed Interpretation," FASB states that the key issue concerns the degree of discretion that the organization has over assets received. For an organization to account for assets received as contributions, they must be able to choose how they will be used and "specifically, that choice must include the discretion to select the beneficiary." Although this interpretation has not yet been issued in its final form, it is not likely to be substantially modified.

Agency transactions are not reported in the statement of activities. However, they must be reported in the statement of cash flows of the organization as an operating activity.

Pell grants and similar financial aid programs

Question: Should Pell grants be reflected as agency transactions? What about other noncampus-based government financial aid programs?

Answer: Pell grants are received by students through the college or university they attend. The grants are based on a financial need analysis, and the organization awards the grant based on an indexed table and other factors. The organization has no decision-making responsibility. Other noncampus-based financial aid usually operates in this fashion, including Stafford student loans, direct lending, and state-based programs. Since the institution facilitates transfers of benefits to third parties, these transactions should be intermediary transactions and not contributions. These transactions should not be reflected in the statement of activities, and any amounts not distributed at the reporting date should be reflected as liabilities in the statement of financial position.

(ii) Part Contribution/Part Exchange

Question: Can a transaction be partly a contribution and partly an exchange transaction?

Answer: Yes. Some examples of transactions that are part contribution and part exchange

are a contractor building a new building for the cost of the materials only, a corporation renting space to a NPO at a fraction of commercial rates, a charitable remainder trust, or a bargain sale.

(iii) Government Transactions

Recording of government contracts

Question: How should government contracts be reflected or reported in the financial statements?

Answer: Government contracts must be evaluated on an individual basis. Each government agency may have different requirements which, when evaluated, will determine whether the transaction qualifies as an exchange, a contribution, or an agency (intermediary) transaction. For example, a Defense Department contract for specific research would likely be an exchange transaction, while a National Endowment for the Arts grant for general support would probably be a contribution. Many states provide funding to private colleges and universities within their state for general support of operations. Depending on their terms and conditions, these may well be classified as contributions. General appropriations by cities or municipalities for general support of an organization may be another example of a contribution. Most contracts and research grants are exchange transactions.

Subcontractor elements of grants and contracts (e.g., the grant recipient subcontracts with another entity to perform specific elements of a grant or contract) generally have the elements of exchange transactions that are recognized as cost elements of the transaction rather than as an intermediary transaction.

Government agreement signed near year-end

Question: If an organization has signed a contract with a government agency as of or just prior to the end of the year, how should the agreement be reported?

Answer: The agreement must be reviewed to determine if it qualifies as a contribution or an exchange transaction. If the transaction is a contribution, the entity should record the transaction as a temporarily restricted contribution in the financial statements. If the transaction is an exchange transaction and no cash has been received, it is the equivalent of "backlog" for a manufacturing organization and should not be reflected in the financial statements. If cash has been received, it should be accounted for as a refundable advance. Disclosure of the type and amount of these contracts, in supplemental management reports, may provide significant information to resource providers.

(iv) Materiality

Recording pledges

Question: Is materiality a consideration in the decision to record pledges? If so, how do we determine it?

Answer: Materiality is normally a consideration in any accounting transaction. Materiality cannot be defined as a single number. If the promise is in support of current operations, its relationship to the total costs of those operations should be considered. Some

Figure 3

Indicators Useful for Distinguishing Contributions from Agency Transactions

Indicator	Contribution	Agency Transaction
NPO's assertions in soliciting assets	NPO solicits assets in support of its own activities	NPO solicits assets for the specific purpose of passing them on to a third-party recipient, or NPO is not substantially involved in the solicitation
Form of assets	NPO changes the form of assets (e. g., from cash to goods or services)	NPO passes assets through to a third-party recipient without changing their form
Legal title to assets	NPO obtains legal title	NPO passes assets through to a third-party recipient without changing their form
Purpose of transfer	NPO regularly carries out the kinds of programs that the assets are intended to support	NPO does not carry out or intend to carry out such programs
Knowledge of recipient	Resource provider does not know specific recipient	NPO and recipient are under common control, have overlapping boards or management, or share facilities or professional advisers

institutions have suggested applying different levels of materiality if the institution has relied on a gift to either raise other funds (a matching program) or to build a building. But materiality, or lack thereof, also can be used to rationalize not examining large numbers of small pledges and therefore excluding them from the decision process for recording.

3. Conditional Contributions

Differentiating between conditional and unconditional promises to give

Question: What is the difference between an unconditional and a conditional promise to give?

Answer: In a conditional promise to give, the donor imposes a condition on the gift that affects the timing of recognition. A donor-imposed condition specifies a future and uncertain event on which the contribution depends. The condition is a barrier that must be overcome before a promised gift is considered a contribution. Assets received subject to conditions are recognized as refundable advances until the conditions have been substantially met. On the other hand, unconditional promises to give are recognized as revenues or gains in the period received.

Conditional pledges

Question: What are some examples of a conditional pledge?

Answer: A matching grant would be an example of a conditional promise, as would a promise to give for a building that the institution had not yet decided to build. A condition must be based upon a future and uncertain event. Another example would be a promise to give cash in support of a proposed program. This would be recognized when the decision is made that the program will be undertaken.

A. Specifies a Future and Uncertain Event

Death

Question: Is death a condition?

Answer: Death is not considered a condition. Even though it will occur at an uncertain time in the future, it is not an uncertain event.

B. Not Recognized as an Increase in Net Assets Until Condition Is Met

While the amounts of such gifts are to be disclosed in notes to the financial statements, conditional gifts are not recorded until the conditions are fulfilled.

Classifying challenge grants

Question: Should challenge grants always be considered conditional promises?

Answer: If the possibility that a challenge would not be met is remote, then it would be considered an unconditional promise.

Matching gifts—conditions met in phases

Question: What happens when a condition is met in phases?

Answer: A promise may contain a condition, such as, "I will match each dollar raised by your organization to a maximum of $100,000." The appropriate accounting recognition should be to record the contribution as each dollar is raised.

However, if the promise to give stipulates that "I will give $100,000 if you raise $100,000 in the next six months," the pledge receivable should be recorded when the possibility of not meeting the $100,000 goal is considered remote. In this case, if the organization raised $95,000 in the first month, it would be reasonable to assume that the match would be completed. Conditional promises to give should not be recognized until the conditions are substantially met.

The same concept applies to the donor when determining when to record a liability for contributions made.

4. Restricted Contributions

Differentiating between conditional and restricted gifts

Question: How is a conditional gift different from a restricted gift?

Answer: A conditional gift differs from a restricted gift in terms of the condition that affects the timing of recognition, not necessarily the purpose for which the contribution may be used. There may be cases where the conditional promise to give also contains a restriction. The conditional nature of the gift determines the timing of recognition while the restrictive nature determines the period or type of use. For example, "I will give $100,000 if the university raises a comparable amount" is a conditional gift whereas "I will give $100,000 to be used for a history conference" is a restricted contribution.

Nature of restrictions

Question: When a donor imposes a restriction on a contribution, are an organization's net assets considered restricted?

Answer: Normally, no. Donor-imposed restrictions generally apply to net assets. However, donors may also restrict specific assets as to use (for example, a building contributed as a rehabilitation clinic) or as to time (for example, securities contributed that must be held in perpetuity).

A. Restrictions by Donor

Legally, only the donor can place a restriction on a gift, but this does not constitute a change nor is it really an accounting issue. The institution may choose to "designate" the purpose for which an otherwise unrestricted gift is to be used, and this may be treated within the institution as if it were restricted. However, it can be "undesignated" just as easily at some future point. Designated funds are a subset of unrestricted resources for external reporting purposes.

Implicit restrictions

Question: What are some examples of implicit factors that would make a contribution restricted even though the donor did not explicitly state the restriction?

Answer: If a donor gave money to a campaign to raise funds for a new building, it would be implicitly assumed that the contribution was for that building, even though the gift restriction was not stated in writing. The same would be true for gifts given in response to solicitations for endowments or other specified purposes.

B. Restrictions Related to the Passage of Time

Time-restricted contributions

Question: How should the following be recorded:

(a) A donor promises to give $1 million today and stipulates that the amount will be paid over the next five years and should be used for operations.

(b) A donor promises to give $1 million today and stipulates that it is to be used for a current year operating project. The promise will be paid over the next five years.

Answer: (a) It is implicit in the pledge that the donation is for the five years in which it is

payable. It should be recorded, at its net present value, as a temporarily restricted contribution and reclassified into unrestricted net assets on a ratable basis over the next five years. (b) It is explicit in the pledge that the donation is for a current year operating project. It should be recorded, at its net present value, as an unrestricted contribution upon receipt of the promise.

C. Specifying the Use of Net Assets

Restrictions of a general nature

Question: How should an organization report gifts to be used at the discretion of the president, a director, a curator, a department chair, or a professor?

Answer: These types of donations should be considered unrestricted contributions. The donor has not imposed a restriction that it should be used for a specific purpose or held by the organization for a certain period of time. Limitations or restrictions of a general nature that are inherent in the normal activities of the organization do not require classification as temporarily or permanently restricted. Examples of other similar unrestricted contributions include gifts to the history department or gifts to be used by the library. While these types of contributions should be classified as unrestricted, the recipient may still categorize them as designated within the unrestricted net asset category.

Types of giving

Basically, there are four types of giving, as shown in the matrix below:

	Unconditional	Conditional
Unrestricted	1	3
Restricted	2	4

Type 1: unconditional, unrestricted

- Given without conditions or restrictions
- Full discretion on when and how contributed assets can be used
- Recognized as unrestricted support when received

Example of type 1 giving: "I give $ 1 million to the university"

Type 2: unconditional , restricted

- Given for a specific purpose or specific time
- Use of the contributed assets limited by donor
- Restriction may be temporary or permanent
- Contribution recognized as restricted support when received

Examples of type 2 giving: "I give $1 million to the university for a guest lecture program."
"I give $1 million to the university to endow a library book fund."

Type 3 : conditional, unrestricted

- Donor has set up a barrier which must be overcome for the organization to have access to the contribution
- Once the barrier is overcome, the gift can be used for any purpose
- Contribution is not recognized until the condition is substantially met

Example of type 3 giving: "I give $1 million to the university if other donors match my contributions."

Type 4: conditional, restricted

- Donor has set up a barrier to overcome and has specified how it is to be used
- Similar to Type 3, recognized when condition is substantially met as either temporarily or permanently restricted

Examples of type 4 giving: "I will give $1 million if the university agrees to build a new gymnasium."
"I will give $1 million to endow a new business school professorship if other alumni will give an equal amount to the school."

5. Measuring and Accounting for Promises to Give

A. Conditions Mandating the Recording of Gifts

(i) Promise Exists

Oral communications as promises

Question: Can oral communications, such as those received in a phonathon, be considered unconditional promises?

Answer: If the person receiving the oral communication prepares documentation indicating the amount of the promise; when, where, and to whom the promise was made; and whether it was restricted or unrestricted, this should meet FASB's documentation standard. If this information is verifiable (whether or not it is actually verified), it should be considered a recordable promise for statement purposes.

(ii) Documentation Indicates a Legally Enforceable Intent

Documentation for promises

Question: What documentation is required to support the recognition of a promise to give?

Answer: Statement 116 is explicit that a promise can be written or oral; however, evidence in the form of verifiable documentation to support that the promise was made must exist. Such documentation is usually in the form of signed pledge cards or other written correspondence. However, records of telephone or other conversations and logs of promises made orally that are verifiable would also suffice as adequate documentation.

Unconditional promises to give

Question: Do unconditional promises have to be legally enforceable?

Answer: FASB does not include "legally enforceable" in the description of an unconditional promise. However, FASB does indicate that if there is any question as to whether a communication is a promise or a communication of intent, it is considered a recordable promise if it is legally enforceable.

Contributions not recorded

Question: Must all contributions be recorded in the financial statements?

Answer: Generally, yes. However, contributed services that do not meet the definition in paragraph 9 of Statement 116 should not be recorded. Conditional promises should not be recorded until the condition has been satisfied. Major uncertainties about the value of a contribution should also be taken into account in deciding whether to record a contribution. Paragraph 84 of Statement 116 indicates that items such as flora, fauna, and photographs may have no value or highly restricted value and should not be recorded.

Matching gifts

Question: If we receive a gift from someone whose employer has a matching gift program, should the match be recorded as a promise?

Answer: In general, most institutions would hold that it was a conditional gift since it would not meet the test of legal enforceability. While many companies have a long history of making such matches, there is nothing that binds them to do so. Accordingly, it would not be recorded. However, if the institution has completed the appropriate forms from the company for the match, that probably would change the circumstances and make the match recordable.

(iii) History of Orally Made Pledges and a Pattern or Collection Exists

Pledges to annual giving campaigns

Question: How should institutions handle pledges made during phonathons for the annual giving fund-raising effort?

Answer: Annual phonathon record keeping probably does not have to be changed. The only question about these pledges comes at the end of the fiscal year when the institution must determine how any unpaid pledges should be recorded on the balance sheet. If the phonathon was early in the school year, chances are that any unpaid pledges may not be collectible and therefore need not be recorded.

B. Promise Versus Statement of Intent

Distinguishing between a promise and a statement of intent

Question: How do you differentiate between a statement of intent and an unconditional promise?

Answer: Generally, if a communication leaves it open to the donor to change his or her mind about the giving of a future contribution, the communication should be considered a statement of intent. If the communication is specific as to the amount and the donor does not reserve any right to reduce or withdraw the promise to give, it should be considered an unconditional promise.

For example, a bequest intention is not an unconditional promise because the individual can change his or her mind. A life insurance policy for which the institution is named owner and irrevocable beneficiary is an unconditional promise.

Question: More clarity is needed between a promise and statement of intent. Can semantics really change the nature of a transaction?

Answer: Sorry, but "semantics" is the name of the legal game. "I promise" has a different connotation legally than "I desire" or "I wish." The first is an unconditional promise while the second is a statement of intent. The same thing happens with restricted versus unrestricted uses: "I want my funds to be used" mandates a restricted purpose, whereas "I desire my funds to be used" is a request that need not be honored. This is known as a precatory declaration. While institutions may choose to follow a public policy of adhering to precatory declarations, that does not change their legal nature.

Interest in a will

Question: Does notification by a donor that the organization is a beneficiary in a will require recognition of a contribution in the financial statements?

Answer: An organization will often be notified that it is a beneficiary in a will. Such notification by a donor is merely an intention to give and does not meet the criteria in Statement 116 regarding an unconditional promise to give. A will is a legal document that may be changed at any time until the death of the donor. In the event of death, the organization would recognize a contribution of its valid interest in the estate when notified by the appropriate court.

C. Recognition of Unconditional Promises as Revenue in the Year of the Pledge

Classifying gifts

Question: Who makes the decision on whether a pledge is unrestricted, temporarily restricted, or permanently restricted?

Answer: There is no single answer for all institutions. The decision should be based on the supporting documentation. However, it should be recognized that donors seldom use clear and distinct language. In many cases some level of interpretation will be needed. At some institutions, this decision may be made by a committee representing counsel, accounting, development, etc. In other cases, the decision is made by a single individual, such as the controller or legal officer.

Defining gifts by net asset class

Question: What are some examples of unrestricted, temporarily restricted, and permanently restricted gifts?

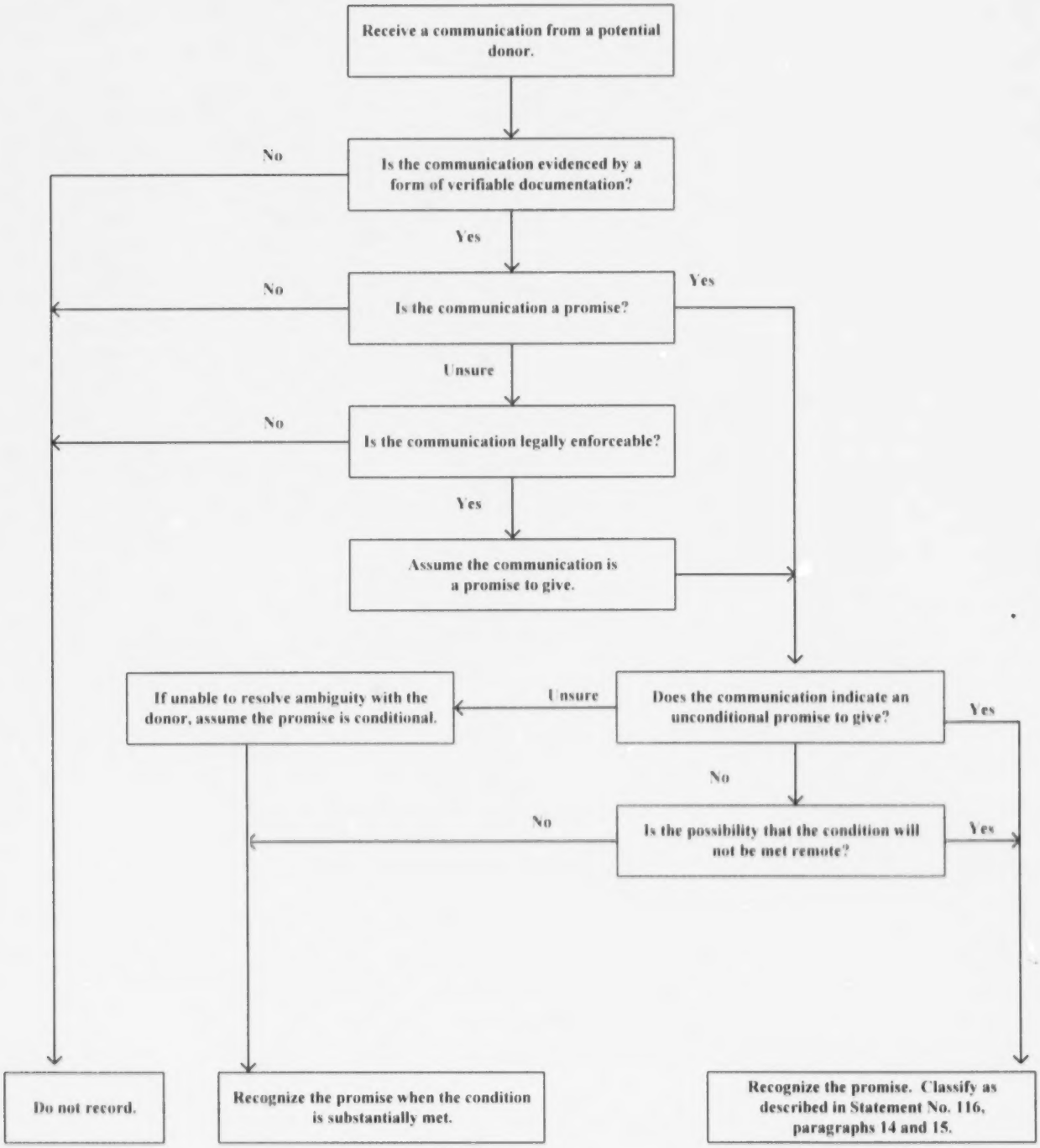
Answer: Contributions received for specific purposes (such as to send the choir to Europe or to buy a new software system for the library) that are not expected to be expended in the same year that they are received would be classified and reported as temporarily restricted contributions. Also, a gift received with a time restriction that it could not be spent until some future fiscal year would be classified as temporarily restricted.

Contributions received with restrictions that the principal can never be spent, such as for endowment or loan funds, would be classified as permanently restricted.

The classification of net assets and revenues as either unrestricted, temporarily restricted, or permanently restricted depends on the existence or absence of donor-imposed restric-

Figure 4

Identifying Promises to Give


Receive a communication from a potential donor.
Is the communication evidenced by a form of verifiable documentation?
No
Yes
Is the communication a promise?
No
Yes
Unsure
Is the communication legally enforceable?
No
Yes
Assume the communication is a promise to give.
Does the communication indicate an unconditional promise to give?
Unsure
If unable to resolve ambiguity with the donor, assume the promise is conditional.
Yes
No
Is the possibility that the condition will not be met remote?
No
Yes
Do not record.
Recognize the promise when the condition is substantially met.
Recognize the promise. Classify as described in Statement No. 116, paragraphs 14 and 15.

tions. Therefore, resources received in exchange transactions are unrestricted revenues and net assets, even in circumstances in which resource providers place limitations on the use of the resources. For example, resources received from the governments in exchange transactions should be reported as unrestricted revenues and net assets, because those limitations are not donor-imposed restrictions on contributions.

Classifying contributions

Question: Statement 116 permits an institution to adopt a policy whereby donor-restricted contributions, whose restrictions are met in the same reporting period, may be reported as unrestricted support in the institution's financial statements. If such a policy is adopted, how should the development office classify these restricted gifts in its reports to the financial office?

Answer: A reporting plan should be worked out by the development office and the finance office whereby contributions of this type are recognized by the development office as being received for a specific purpose, but are recognized by the finance office as unrestricted for financial statement classification purposes. If you currently report to the finance office restrictions on all gifts, your reporting process should be adequate.

Contributions received with restrictions that are not expected to be fulfilled within the same reporting period should be classified as temporarily restricted.

Question: When such gifts are classified as unrestricted, won't the financial records be distorted and suggest that the institution has more unrestricted financial support to spend for general operational needs than it really has?

Answer: Quite the contrary. FASB would contend that these contributions are unrestricted, or at least that their restrictions are lifted shortly after their receipt; therefore, this classification scheme actually provides a more accurate picture of the resources available to the institution.

Recording multiyear pledges

Question: If a donor indicates an intention to pay a pledge over the next three years, what does the institution assume about when it will be received?

Answer: Unless specific information is available, the assumption is that the gift will be received ratably over the three-year period.

Timing for recording an unconditional promise

Question: When should an unconditional promise to give be reported as contribution revenue and receivable by the recipient? At what point should it be recorded as a liability by the donor?

Answer: An unconditional promise to give should be recognized by the donor and the donee when sufficient verifiable evidence indicates a promise was made. "I promise to give $100 to the annual fund campaign" is an example of an unconditional promise that should be recorded by the donor and donee when the promise is communicated.

An intention to contribute should not be considered an unconditional promise if it is not legally enforceable. "In connection with your planning, it would be my intention, if I am

able, to contribute $100 before December 31," is an example of an intention that should not be recorded until the cash is received or the donor makes a promise.

Reporting unconditional promises

Question: Generally, when should the development office report unconditional promises to the finance office? As they occur, quarterly, or at the end of the fiscal year?

Answer: The answer depends upon the accounting records that the finance office has set up for promises. In any case, the minimum requirement would be annually at the end of the fiscal year.

Reporting unconditional promises to annual giving

Question: If the development office is reporting unconditional promises to the finance office at the end of the fiscal year, wouldn't that automatically exclude the need to report any such promises made to the annual giving effort?

Answer: This would be true only if the promises received had been paid. If they had not been paid at year-end and were considered collectible, they would need to be recorded or at least reviewed for materiality and collectibility to determine if recording is appropriate.

Recording unconditional promises to give in the future

Question: How should unconditional promises that are expected to be received more than one year after the financial date be recorded?

Answer: If the contribution is an unconditional promise to give cash more than one year after the financial statement date, it should be measured at the present value of the expected cash flows. For example, a promise to give with payments due in future periods should be reflected as restricted support (temporarily restricted category) at the net present value unless the explicit donor stipulations surrounding the receipt of the promise make it clear that the donor intended it to be used to support the current period activities.

If the contribution is an unconditional promise to give noncash assets more than one year after the financial statement date, it should be measured at the present value of the assets' fair value at the date the assets are expected to be received. If the assets' expected fair value is difficult to determine, the current fair value may be the best estimate of its fair value.

Meeting matching requirements with institutional funds

Question: If a donor stipulates that he or she will donate $100,000 of permanently restricted funds if the organization will match it, how should the organization record the match?

Answer: According to Statement 116, the definition of permanently restricted net assets includes reclassifications from (or to) other classes of net assets as a consequence of donor-imposed stipulations. The $100,000 needed to match the donor-imposed restriction, if not matched by other restricted contributions, could be approved by the board, and an amount that would meet the matching requirements should be reclassified to permanently restricted net assets. Subsequent reclassification from permanently restricted net assets without specific donor approval would not be permitted.

Action by governing board

Question: Can an organization's governing board permanently restrict contributions or realized gains on permanently restricted endowment gifts?

Answer: Only donors or federal or state laws may permanently restrict contributions or realized gains. A board may designate net assets, but only with unrestricted net assets. The exception to this rule is the reclassification of funds to meet a matching requirement as defined in the previous Q & A.

6. Other Kinds of Gifts

A. Deferred Giving Arrangements (Split Interest Gifts)

Some donors enter into trusts or other arrangements under which NPOs receive benefits that are shared with other beneficiaries. These are known as "split interest agreements." There are five different types of such agreements—charitable lead trusts, perpetual trusts held by third parties, charitable remainder trusts, charitable gift annuities, and pooled (life) income funds.

Under a split interest agreement, a donor makes an initial gift to a trust or directly to the NPO and the NPO has a beneficial interest but is not the sole beneficiary. The time period covered by the agreement may be either a specified number of years, in perpetuity, or over the remaining life of an individual or individuals designated by the donor. The assets are invested and administered by the organization, or a separately designated trustee or fiscal agent, and distributions are made to beneficiaries during the life of the agreement. At the end of the agreement term, the remaining assets become the property of either the NPO or another beneficiary.

Under an agreement known as a "lead interest," the NPO receives distributions during the agreement's term. In contrast, where a "remainder interest" exists, either the donor or someone designated by the donor receives distribution during the agreement's term and the nonprofit organization receives all or a portion of the remaining assets at the end of the term.

Assets received under split interest agreements should be recorded at their fair value. This transaction is part contribution and part exchange. The contribution portion of the agreement (i.e., the part that benefits the NPO) should be recognized as revenue or as gain. The exchange portion, that portion payable to another beneficiary, should be recognized as a liability.

(i) Charitable Gift Annuities

A charitable gift annuity is an agreement between a donor and a nonprofit in which the donor contributes assets to the organization in exchange for a promise by the organization to pay a fixed amount for a specified period of time to either the donor or individuals designated by the donor.

(ii) Pooled (Life) Income

A nonprofit organization creates a pooled income fund, like a mutual fund, which is divided into units. A donor's contribution purchases units in the pooled fund based on market value of the total fund at the time of the gift. The donor, or a donor-designated beneficiary, is paid

the income earned by the assigned units' share of the total fund. Upon the death of the income beneficiary, the value of the assigned units reverts to the nonprofit organization.

(iii) Charitable Lead Trust

A charitable lead trust is an agreement in which the donor establishes and funds a trust with specific distributions to be made to a designated nonprofit for a specified time period. Upon termination of the time period, the remainder of the assets is paid to either the donor or to beneficiaries designated by the donor. If the distributions are a fixed dollar amount, it is known as a charitable lead annuity trust (CLAT), or a charitable lead unitrust (CLUT), if the distribution is based on a fixed percentage of the trust's market value determined annually.

(iv) Charitable Remainder Trust

A charitable remainder trust is an agreement in which the donor establishes a fund with specified distributions to be made to a designated beneficiary over the term of the trust, at the end of which the NPO receives the remaining assets. If the distributions to the beneficiaries are for a specific dollar amount, it is known as a charitable remainder annuity trust (CRAT). If the distributions are for a specified percentage of the trust's market value determined annually, it is known as a charitable remainder unitrust (CRUT).

In the past, gift annuities were to be recorded at their net present value, which is the value today of the portion of the assets that would become available to the institution at the time the annuity agreement terminated, based on the life expectancy of the annuitant. Other types of split interest gifts were to be recorded at their value at the time received. Although Statement No. 116 does not contain any specific instructions, a significant change will be required, as described in the proposed AICPA audit guide. With the implementation of Statement 116, all split interest gifts are to be recorded at their present value. For example, a gift of a pooled income fund would be discounted to its net present value based on the life expectancy of the income beneficiaries. Over the ensuing years, that value would be adjusted annually until the present value and market value agreed, presumably at the time the income payments ceased due to the death of the income beneficiary.

Recording split interest gifts

> **Question**: An organization received certain investment assets from a donor. The donor specified that during his lifetime all income generated by the investments must be paid to him. Upon his death, the principal of the investment must be held as an endowment. Where and how should this transaction be recorded in the financial statements?
>
> **Answer**: Based on the donor's restriction, the contribution should be recorded in the permanently restricted net asset category at the net present value of the amount expected to be received upon the death of the donor. The difference between the fair value of the investment at the date of the gift and the net present value of the amount expected to be received is reflected as a discount.
>
> In contrast, if the donor had not stipulated that the funds must be held as an endowment, the amounts would be classified as temporarily restricted assets at the net present value of the amount expected to be received because there is an inherent time restriction in the gift.

B. Perpetual Trusts Held By Others

Recording funds held in trust by others

Question: Should an organization record funds held in trust for its benefit by others?

Answer: Donors establish irrevocable trusts from which the organization is to receive the income in perpetuity but the principal is held in trust by another entity, usually a bank, and will never be available to the organization. The perpetual stream of income should be reviewed by the organization as a promise to give by the donor, and therefore it should be recorded at fair value, like any other promise to give.

The net present value of the income stream should be recorded as a contribution. Generally, it is acceptable to value the contribution at the fair value of the principal of the trust. Given the nature of the promise, it is acceptable to reflect the contribution as permanently restricted (like an endowment) and adjust its value annually using the same method used to record the original promise. The income should be recorded based on the donor's stipulations.

Question: Statement 116 has been interpreted to say that funds held in trust by others should be recorded. Since colleges and universities will never have control over these assets, how can that be justified?

Answer: In booking a fund held in trust by others, the present value of the future revenue stream is recorded, not the assets that produce that revenue stream. It has been suggested that a reasonable definition of that future revenue stream would be the current value of the assets in the trust, but there is nothing in Statement 116 that requires that definition. Indeed, some institutions report having difficulty obtaining the value from the trustees. In those cases, the institution may wish to use alternative means of valuation, such as applying an appropriate discount rate to the annual revenue stream.

Recording revocable trusts

Question: If an organization receives assets in the form of a revocable trust, how should the trust be reflected in the financial statements?

Answer: Revocable trusts are conditional transfers and should be reflected both as an asset and a refundable advance.

C. Life Insurance

Gifts of life insurance policies

Question: An organization receives a life insurance policy as a gift from a donor and has also been named as the beneficiary of the life insurance policy. The life insurance policy premiums are to be paid out of the increase in the cash surrender value during the holding period. May the premiums be netted against the increase in the cash surrender value for financial reporting purposes?

Answer: The cash surrender value of the policy is a contribution. The premiums related to the policy are an expense as incurred. The increase in the cash surrender value should be recorded as earned and may be recorded net of the insurance premium expense. This reflects the substance of the donor's intent in contributing the insurance policy.

D. Contributed Services

Question: When should contributed services be recorded as contribution revenue?

Answer: Contributed services should be reported as contribution revenue and as assets only if the services (a) create or enhance a nonfinancial (i.e., non-monetary) asset, or (b) would (1) typically need to be purchased by the organization if not provided by contribution, (2) require specialized skills, and (3) be provided by individuals with those skills.

For example, if parents of children at a daycare center contribute materials to build a playground, the materials should be recognized as a contribution. If the parents volunteer to perform general office services on an as-needed basis, these contributed services should not be recognized since the services do not require specialized skills. However, if the parent were a doctor or a nurse and provided a service, such as mandatory physical examinations, contributed services should be recognized.

Contributed services should be recognized if employees of separately governed affiliated organizations regularly perform services, other than in an advisory capacity, under the direction of the recipient organization.

The notes to the financial statements should contain information describing the programs or activities for which contributed services are received and used and the amount recognized as revenues for the period. Organizations are encouraged but not required to disclose the fair value of contributed services received but not recognized.

Contribution of future services

Question: Should promises to give future services be recorded as contribution revenues?

Answer: Promises to give future services are generally considered conditional because they are based on the uncertain future availability of specific individuals to provide those services and should not be recognized until performed.

Contributed services by religious orders

Question: Will the contributed services of faculty and staff who are members of religious orders be reported as gift income on the institution's financial records? Will that typically be handled solely by the finance office or will the development office also be involved in the recording?

Answer: Where it is determined that there has been a contribution of services by faculty and staff, the fair value of their services would be recorded as contribution revenue, net of any expenses incurred for their services. This is the one area where colleges and universities have tended to record contributed services. This calculation would presumably be made by the finance office, perhaps in consultation with the development office, but more likely with academic administrators.

Services contributed at cost

Question: When an individual provides services such as constructing a facility at cost rather than at the fair market value of the services, which amount does FASB expect to be reported as gift income?

Answer: The difference between the fair market value of the asset received and the cost charged to the institution would be considered a contribution under the new FASB standards.

E. Collections

Question: Will the new FASB standards relating to contributions of works of art, historical treasures, and similar items have any impact on the development office?

Answer: No. They should not have any impact on development operations, but the business office will have to decide whether contributions of this type need to be reported in the financial statements as contributions.

Recording works of arts and other collections

Question: Many nonprofit organizations are recipients of various works of art and collections. Is the nonprofit organization required to recognize these collection items as contributions?

Answer: If the contributed collections received by the organization meet the definition of a collection in Statement 116, the options available to account for the collections may be used. Appendix D of Statement 116 defines collections as follows:

> Works of art, historical treasures, or similar assets that are (a) held for public exhibition, education, or research in furtherance of public service rather than financial gain, (b) protected, kept unencumbered, cared for, and preserved, and (c) subject to an organizational policy that requires the proceeds of items that are sold to be used to acquire other items for collections.

If an organization receives a valuable painting, a coin collection, a statue, or other works of art or collections and capitalization is required, they should be recognized as assets and contributions at fair value. When implementing the requirements of Statement 116, organizations should review the accounting for these types of items received in the past.

F. Contributed Facilities and Equipment

Recording contributions of long-lived assets

Question: How should the contributions of long-lived assets, such as land, buildings, and equipment, be recorded?

Answer: There are some choices. If the donor specified how the donations are to be used or for what length of time, those gifts should be reported as temporarily restricted. If the donor doesn't place either a purpose or time restriction, the organization has two alternatives. If the organization chooses to impose no time restriction, the gift is recorded when received as unrestricted revenue.

However, if the institution chooses to imply a time restriction that expires over the life of the asset, it should be recorded as temporarily restricted. This policy must be applied consistently from year to year and must be disclosed in the notes to the financial statements.

Recording contributed facilities

Question: How should an organization record the use of donated facilities, such as a building?

Answer: If an organization uses facilities rent-free or at a price below the market value, it should recognize the contribution revenues and expenses in the period received and used.

If an organization receives or uses facilities under lease agreements that are below market value or at a nominal amount, the lease should be reviewed for potential capitalization under the requirements of Statement No. 13, *Accounting for Leases*. In evaluating the lease for capitalization, the present value of the minimum lease payments should be based upon the fair market value of the payments rather than their contractual amount. If capitalization is required, the lower of the present value of the lease payment or the fair value of the asset should be reflected as a contribution. The organization should also include the appropriate disclosures required by Statement No. 13.

If an organization has not previously recognized facilities under this guidance, it should consider the original date of the agreement and estimate the values based on conditions in effect at that time. The organization also considers depreciation expense from the date of the original agreement.

Capitalizing or expensing capital gifts

Question: Under what circumstances should a contribution of a capital asset be expensed?

Answer: An asset donated to an organization that is required to be returned upon the expiration of a specific project or grant should be recognized as contribution revenue and expensed over the period of the project. An asset that has no service potential beyond the specific purpose for which it was donated should be expensed over the period of the grant or project.

G. Contributions to Acquire Fixed Assets

Contributions of cash or other assets restricted to the purchase of long-lived assets are always purpose-restricted and could also be time-restricted if the donor stated how long the assets purchased were to be held.

Recording gifts to purchase fixed assets

Question: If an organization receives cash or other assets to be used to purchase fixed assets, how should the contributions be recorded?

Answer: Cash or other financial assets restricted by the donor to be used to purchase fixed assets should be recorded as contributions under the temporarily restricted net assets category. Upon fulfillment of the restriction (purchase of construction of the asset and placement in service), the net assets should be reclassified to the net asset category in accordance with the organization's policy governing time restrictions on fixed assets acquired with gifts of cash or other assets.

Contributions for buildings

Question: How should an organization record a promise received in a capital campaign for a building that is not scheduled for construction until some time in the future?

Answer: Unconditional promises should be reflected as revenues and receivables when the promise is made. The contribution should be recorded as temporarily restricted at its net present value because it is both purpose and time restricted. The amortization of the discount should be reflected as an additional contribution.

In the statement of cash flows, this would be reflected as a financing activity.

Capital Bequests

Question: What do you do if the institution relies on a promise to build a building and the promise is backed by a donor's bequest?

Answer: The institution needs to recognize that the donor could change his or her will and the institution could be left with an unpaid promise, or economic conditions could change so that the donor's estate was incapable of honoring the promise. In short, it's a gamble that the institution has to decide whether or not to take, and it would be wise to identify alternate resources just in case. Generally, a promise backed by a will would not be recorded. However, if the institution feels it has sufficient documentation in support of the promise, including the right to make a claim against the donor's estate, it may choose to recognize the promise when it is made.

H. Gifts-in-Kind

Recording gifts-in-kind

Question: How should gifts-in-kind be recorded?

Answer: Gifts-in-kind should be measured at fair value on the date of receipt. Fair value should be based on the quantity received after any applicable discounts have been considered. For example, computers and other donated equipment should be valued at what it would cost the institution to acquire them after allowance for educational discounts, not at retail price. The same concepts for determining whether a promise to give cash is an unconditional contribution should be used to determine when and if gifts-in-kind should be recorded. Depending on the nature of the gift, unconditional gifts-in-kind should be capitalized.

If the assets are sold at a later date, any gain or loss should be recognized based on the nature of the assets used by the organization. For example, gifts used for auctions or other fund-raising activities should result in the recognition of an additional contribution or an adjustment to contributions. If they are sold in an exchange transaction, such as inventory in a thrift store, the appropriate accounting should reflect revenue and cost for that type of transaction. Items used as fixed assets, if sold, should result in a gain or loss on sale.

7. Other Considerations

A. Uncollectibles

(i) Allowance

Setting the allowance for uncollectibles

Question: How should an organization determine the allowance for uncollectible contributions receivable? Once an estimate of uncollectible amounts has been established, how should the adjustments to the original estimate be recorded?

Answer: The allowance for uncollectible contributions receivable should be based on a reasonable methodology. In determining an appropriate allowance, an organization may

consider factors such as past collections history, age of the receivable, credit standing of the donor, the organization's policy on enforcement of promises, and other factors.

Contributions from a mass appeal should be recorded at the estimated realizable value. Any differences between the estimated and actual uncollectible amounts should be reported as a change in the net asset category in which the contribution revenue was originally reported or in the category in which the net assets are reflected.

Some organizations' experience would indicate a pattern of donor fulfillment of pledge commitments such as the following:

- Annual fund drives often result in a very high percentage of payments received by December 31. If the organization is on a fiscal year and the drive is conducted earlier in the year, promises unfulfilled at year-end are sometimes an indicator of uncollectibility.
- Stratification of pledges by purpose, term, and donor characteristics provides significant information that will assist in establishing an estimate for uncollectible contributions.
- General experience may indicate a high degree of collection for specific capital campaigns, such as buildings or specific endowments.

Reserve for uncollectible pledges

Question: What impact does the reserve have on the development office?

Answer: The reserve fund established by the finance office for uncollectible pledges does not affect the development office. However, the chief development officer should be involved in determining the appropriate size of this reserve.

(ii) Write-offs

Establishing a write-off policy

Question: What about write-offs and adjustments? Who makes the decision? What kind of documentation is required?

Answer: Periodically, at least annually, outstanding pledges should be reviewed for collectibility. In some cases, the amount may need to be adjusted, either up or down, and in other cases may need to be written off. While the final responsibility for deciding should rest with the business officer, the development office will play a critical role. Documentation might include correspondence with the donor, but is more likely to be internal memorandum identifying the reasons for the decision.

Write off of unconditional promises

Question: Should unconditional promises be written off as uncollectible at the expiration of the promise period?

Answer: Like any other receivable, an unconditional promise should be written off when there is little or no expectation of receiving payment. This could conceivably occur before the due date of the promise.

B. Present Value

(i) Discounting

Setting the discount rate

Question: What discount rate should an organization use when discounting the present value of the future cash flows of a promise to give?

Answer: The interest rate used by an organization to discount future cash flows should be based on a risk-free rate. Consideration should be given to a rate for the same duration as the promise, such as a U.S. debt obligation or other appropriate rates, if those rates meet the requirements of "risk-free." The rate chosen and basis of selection should be disclosed in the financial statements.

In accordance with Accounting Principles Board Opinion No. 21, *Interest on Receivables and Payables,* the discount rate should be determined at the time the unconditional promise to give is recognized and should not be revised when rates change.

In computing the discount, the rate should be applied to the contributions after estimating any allowance for uncollectible amounts.

Discounting split interest gifts

Question: In determining the present value of split interest gifts, what discount rate is recommended?

Answer: Statement 116 states that present value should be determined using a "risk free" rate. A number of institutions have stated that they intend to use the IRS tables' actuarial assumptions and deduction formulas as a reasonable definition of the discount rate, and the AICPA will agree with that approach in their soon-to-be-published audit and accounting guide for nonprofit organizations.

Amortization of discount

Question: If a pledge has been discounted to its present value when received, how is the amount amortized handled in subsequent years?

Answer: The amortized amount would be recovered in subsequent years on a straight line basis and reflected in the financial records as gift income each year.

Question: Does this also apply to the discount of split interest gifts?

Answer: No. The discount of a split interest gift is based on the life expectancy of the income beneficiary. Life expectancy tables do not change in a linear fashion. In effect, the present value of split interest gifts needs to recalculated each year, based on appropriate life expectancy tables. Depending on the number of such gifts, the institution may want to develop a software system for tracking, calculating, and recording the annual changes in split interest gifts.

C. Expiration of Restrictions

Fulfillment of donor-imposed restrictions

Question: How should an organization recognize the fulfillment of donor-imposed restrictions?

Answer: Restrictions on contributions expire when either the stipulated time has elapsed or expenses have been incurred that meet the purpose of the restriction. In general, expenses incurred are presumed to meet the restricted purpose first. Reclassification from temporarily restricted to unrestricted net assets should be reflected in the statement of activities when the restrictions are met, expire, or lapse. If the restrictions are met for only a portion of the temporarily restricted amounts, only that portion should be reclassified. If an expense is incurred for a purpose for which both unrestricted and temporarily restricted net assets are available, a donor-imposed restriction is fulfilled first.

Upon adoption of Statement 116, organizations may elect to implement requirements governing the expiration of donor-imposed restrictions, either prospectively or retroactively. If retroactive application is elected, each organization should review funds previously classified as restricted to determine whether the restrictions have been satisfied and to quantify the amounts to be reclassified to unrestricted net assets.

However, organizations should keep in mind that if an expense is incurred in an exchange transaction or is directly attributable to a specific external source of revenue, this expense should not be considered to have met a donor-imposed restriction. For example, a donor restricts a contribution to underwrite the cost of a specific activity and, as part of an exchange transaction, the organization incurs costs for that activity. These costs are directly related to the exchange transaction. The restricted contribution should be reclassified until other costs that satisfy the restricted purpose have occurred.

An organization may satisfy donor-imposed restrictions in the same reporting period in which the contribution is received. The institution is permitted to adopt a policy of reporting as unrestricted such contributions received for restricted purposes that are spent in the year received. If the organization adopts a policy of reporting such contributions as unrestricted support, it must be disclosed in the financial statements. Further, it must be applied consistently from period to period.

If two or more donor-imposed restrictions are placed on the same contribution, the reclassification from temporarily restricted net assets to unrestricted net assets is recognized in the period in which the last restriction is satisfied.

Impact of change in lifting of restrictions

Question: Will the Statement 116 provision concerning lifting of restrictions have a significant impact on the way we do business?

Answer: It's probably too early to tell. Most institutions are still trying to figure out what they need to change for recognizing promises and how to categorize funds in the categories of permanently restricted, temporarily restricted, and unrestricted. However, some institutions see these accounting rule changes as an opportunity to make significant change. Specifically, some are moving in the direction of mandating that restricted re-

sources are to be used first, which is a substantial change from the past. Some have suggested that this will mark the end of fund accounting as it is now known. Others are more sanguine, feeling there still needs to be a way to ensure that moneys are used as the donors intended and fund accounting is the best way to ensure that this happens.

Restricted funds—budget relief or addition

Question: FASB Statement No. 116 states that if an expense is incurred in the general operating budget of the institution for a purpose for which a donor-imposed restricted contribution has been received, then the restriction has been fulfilled to the extent of the expense incurred.

Doesn't this mean that if a donor makes a contribution restricted to support travel expenses of the English department faculty, that restriction would be fulfilled if a like amount of travel expense were incurred and charged to the department's travel budget? Many institutions now consider such restricted gifts as supplements to the budget rather than budget relief. Will this standard require these institutions to change their policies?

Answer: An institution does not necessarily need to change its policy. Separate funds can continue to be established to hold such contributions, but for financial statement purposes they would be classified as designated funds in unrestricted net assets rather than restricted funds in temporarily restricted net assets.

Lifting of restrictions: the impact on budgeting

Question: Will this change the institution's budget process?

Answer: The new lifting of restriction standards established by FASB need not have an impact on an institution's budget process. However, some institutions, particularly larger ones, may use the new FASB requirements as a means for getting departments to spend restricted resources before unrestricted funds. In those cases, there would be an impact on the budget process.

D. Fund-Raising Costs

Identifying fund-raising costs

Question: Where do you draw the line between fund-raising and more general university relations costs?

Answer: Although there are no hard and fast ground rules, most institutions will probably choose not to allocate executive costs between fund-raising and other activities. In general, most will restrict their definition to those costs specifically budgeted and accounted for as development costs.

Fund-raising expenses

Question: Do fund-raising expenses have to be shown as a separate line item?

Answer: Fund-raising expenses do not have to be shown as a separate line item on the financial statements. If they are not shown as a separate line item, then total fund-raising expenses should be disclosed in the notes to the financial statements.

Premiums related to fund-raising

Question: How should premiums or gifts related to fund-raising be recorded?

Answer: The cost of nominal items given to potential donors as part of a mass fund-raising appeal are fund-raising expenses. The premiums are not provided to the potential donor in exchange for assets contributed, since the premiums may be kept by all those from whom the funds are solicited, regardless of whether a contribution is made. For example, flower seeds or address labels included with a fund-raising solicitation should be recorded as fund-raising costs. Premiums of a nominal value (coffee mugs, posters, books bags, etc.) provided to donors to acknowledge the contribution should also be recognized as fund-raising costs.

E. Special Events

Special event costs

Question: Will an organization be able to net the direct costs of a special event against the revenues of that event? Are there any other types of transactions whereby an organization may present revenues net of related expenses?

Answer: If special events are ongoing and are major or central activities, organizations should report the revenues and expenses as gross. Special events that are peripheral or incidental may be reported either as net or gross. The frequency of the events and the significance of the gross revenues and expenses are elements that help distinguish ongoing and major events from peripheral or incidental events.

An organization may report special events revenues with direct costs deducted on two separate lines, with a subtotal with appropriate descriptions, or as revenue in the revenue section of the statement of activities and expenses in the expense section of the statement of activities. The special events revenues may be part exchange (for the fair value the participant received) and part contribution (for the excess of the payment over that fair value), and the two parts may be reported separately.

An organization should only report special events with direct costs deducted or disclosed parenthetically if the activities are peripheral or incidental. Dinners, social events, and similar activities designed to raise funds or the sale of publications written by members might represent special events.

Special events donations

Question: If a college invites potential donors to attend an event which has a per capita cost of $75, do we have to deduct the cost from any contribution they might make and report the lesser amount as a contribution?

Answer: As described, it would appear that no reduction would need to be made since no contribution was required for them to attend.

F. Membership Activities

Membership development activities

Question: We have organizations within the university that have membership programs, such as the art museum, library, and athletics. Are membership dues contributions or exchange transactions? When is the membership earnings process complete?

Answer: Membership dues often have elements of both a contribution and an exchange transaction, because members may receive tangible or intangible benefits from membership in the organization. It may be difficult to measure the benefits members receive and to judge whether the value received is approximately equal to the dues paid by the member. Accordingly, each transaction should be reviewed and separated into its proper components. To the extent that membership dues are a contribution, immediate recognition is required. If a portion of the membership dues represents the sale of goods, exchange transaction accounting would recognize revenue and cost of sales when the earnings process is complete. Membership dues should be recognized over the term of the membership.

A membership in a civic organization is usually associated with a contribution. A membership in an organization that provides a monthly magazine, rights to activities at reduced or no cost, and similar benefits includes a membership component and is partially an exchange transaction and partially a contribution. Each element could be evaluated as an individual transaction and if the amounts allocated for the magazine and the value of the rights of membership are less than the total amount of the membership, a contribution would be indicated. An organization should carefully consider the financial statement display of these components of revenue.

G. Disclosure Requirements

Government contributions

Question: If some government funding meets the definition of "contribution," does this suggest that the "contributions" line in the financial statement should show separately the various sources of donors? What difference would it make if we continued to show government contributions under "government grants and contracts"?

Answer: There is no requirement to provide a breakdown of contributions by type of donor, although some organizations may choose to do so. It would not make any difference to continue showing government contributions under "government grants and contracts." What is important is that any government contributions be accounted for as "contributions," not as exchange or agency transactions.

Reporting for contributed services

Question: What reporting is required for contributed services?

Answer: The notes to the financial statement should contain information describing the programs or activities for which contributed services are received and used and the amount recognized as revenues for the period. Organizations are encouraged but not required to disclose the fair value of contributed services received but not recognized.

Reporting nonfinancial assets received

Question: How should contributions of nonfinancial assets be recorded?

Answer: Noncash contributions such as gifts of long-lived assets, consumable assets, and donated services that meet the requirements of Statement 116 should be reflected in the statement of activities at their fair market value. Noncash operating, investing, and financing activities should also be disclosed in the financial statements. Required disclosures should be shown on either the face of the statement of cash flows or in the notes to the financial statements.

Display of contributions in the cash flow statement

Question: In what cash flow category should contributions be recorded? Should accounts and contributions receivable be reflected gross or net in the statement of cash flows?

Answer: Cash flows that result from gifts restricted by the donor for long-term purposes, such as endowment or plant, should be presented as financing activities. All other contributions should be presented as operating activities.

Generally, cash flows should be reflected as gross. The change in accounts and contributions receivable is computed using the net receivable amounts (net of the allowance for uncollectibles) when using the indirect method of preparing the cash flow statement and/

Figure 5

Indicators Useful for Determining the Contribution and Exchange Portions of Membership Dues

Indicator	Contribution	Exchange Transaction
Expressed intent concerning purpose of dues payment	The request describes the dues as being used to provide benefits to the nonprofit organization's service beneficiaries	The request describes the dues as providing economic benefits to members or to other organizations or individuals designated by or related to the members
Extent of benefits	The benefits to members are negligible	The substantive benefits to members (publications, admissions, educational programs, special events, etc.) may be available to nonmembers for a fee
NPO's service efforts	The NPO provides service to members and nonmembers	The NPO benefits are provided only to members
Duration of benefits	The duration is not specified	The benefits are provided for a defined period; additional payment of dues is required to extend benefits
Qualifications for membership	Membership is available to the general public	Membership is available only to individuals who meet certain criteria (e.g., requirements to pursue a specific career or to live in a certain area)

or reconciling from the change in net assets to cash provided by operations. When using the direct method, the provision for uncollectible accounts adjusts cash flows for operating expenses, and the gross change in receivables adjusts cash from service recipients or contributors.

Reporting agency transactions

Question: How should agency transactions be reported?

Answer: Resources received in transactions in which the organization is acting as an agent, trustee, or intermediary should be reported as increases in assets and liabilities; subsequent distributions to third-party recipients should be reported as decreases in those accounts. Cash received and paid should be reported as cash flows from operations in a statement of cash flows.

(i) Aging Requirements

Footnotes to the financial statements should disclose a breakdown of contributions receivable by the amounts due within one year, one to five years, and more than five years. Likewise, those footnotes should describe the interest rates used in discounting future gifts to their present value.

(ii) Write-off Requirements

As is true on any allowances for uncollectible accounts, footnotes should identify the amount of the allowance for uncollectible contributions as well as how it was determined.

(iii) Deferred Giving Requirements

Notes to the financial statements should include a description of the general terms of existing split interest agreements, the basis used for recognizing assets (i.e., cost, lower of cost or market, fair market value), and the discount rates and actuarial assumptions used in calculating the present value of the agreements.

H. Accounting Issues

Payments on pledges

Question: In addition to reporting on the amounts of pledges received, don't you also have to report on cash receipts to distinguish those that are payments on pledges previously recorded from those that represent new gifts received during the year?

Answer: Yes. When future promises are recorded, the offset is to a pledge receivable. When payments are made on those pledges, the entry diminishes the receivable and increases cash. No gift would be recognized except for the difference between the amount received and the time-discounted value recorded when the pledge was received.

8. Recommendations

A. Analyze Existing Pledges

Starting the process

Question: Where do we begin?

Answer: Every institution will have their own pattern for the process, to some degree dependent on the quality and quantity of existing information. One approach to designing a program is to begin by making a list of all outstanding pledges in descending order by amount. Then starting with the largest, determine the completeness of supporting documentation. This may well turn into a search process, requiring visits to the president's, vice president's, departmental, and development offices., wherever anyone these offices may have been involved in the efforts that led to the receipt of the pledge. A review of this documentation will lead to classifying some of the pledges as conditional pledges or statements of intent. These can be set to one side. For those remaining, a materiality level should be established to determine whether or not they should be recorded. This will provide the starting point for those to be recorded, for determining the appropriate level of an allowance for uncollectibles, and for aging them by year of expected receipt.

Maximizing pledges recorded

Question: Some institutions seem to be following a plan that would recognize only those few pledges that meet Statement 116 requirements strictly, whereas other institutions are using fairly loose definitions. Why would a college or university choose to pursue an aggressive policy to maximize pledges recorded?

Answer: The impact of recording future promises will be to increase revenues and net assets. For some institutions, this is seen as a way of displaying greater financial stability and improving debt capacity.

Audit considerations for implementing FASB Statement No. 116

Question: What will our auditors be looking for to determine whether we have properly implemented Statement 116?

Answer: Different auditors will have different approaches, but the prime considerations will be documentation of any promises recorded, materiality of amounts, whether included or excluded, and adequacy of the controls surrounding fund-raising.

Auditor concerns

Question: Our auditors are telling us we have to examine every document and record every single pledge. What do we do?

Answer: As with any other accounting issue, you need to start with the basic premise that the financial statements are the institution's not the auditor's and determine institutional policies on a number of issues. For example, are you going to treat all pledges made and paid within the same year as unrestricted and disregard open balances at year-end as probably not collectible, as is typical of most annual alumni fund drives? Will funds

given for restricted purposes and spent within the same year be recorded as unrestricted, or will they be recorded initially as temporarily restricted and then transferred when spent? Do you wish to set a reasonable level for reviewing and determining whether pledges should be recorded? Most institutions have a variety of thresholds for different transactions—accounts payable, capitalization of fixed assets, etc. Decisions regarding contributions will be one more example. For instance, one large institution that raises in excess of $100 million annually has set a minimum of $10,000 for recording pledges. Another has adopted a policy of recording all promises that have been relied on for fund-raising or capital purposes, in effect, recording any challenge gift used for matching purposes or any pledge for a new facility. This should not suggest that all institutions need to have identical policies but rather to illustrate the need for every college to review the implications of Statement 116 on their current policies and practices and decide if they need to be modified.

B. Review Existing Documentation

Modifying pledge documents

Question: Many institutions have developed standard documents to be used with donors. What do you do if the donor wishes to make changes to these documents?

Answer: Most institutions regard such documents as merely a guide and therefore would make whatever changes the donor wished to make, as long as it didn't place the institution in an untenable position of agreeing to do something it didn't wish to do.

Modifying pledge cards

Question: Is there any need for institutions to use the phrase "promise to give" rather than "pledge" on their pledge cards?

Answer: No. When the word "pledge" is used, it should be considered synonymous with "unconditional promise." Therefore, as long as the pledge card carries with it a specific date for fulfillment, there is no reason for changing the current wording.

Question: Should institutions include on pledge cards a place for donors to indicate whether the gift is conditional or unconditional?

Answer: No, this isn't necessary. Most institutions do not receive many conditional promises. When donors want to make conditional promises, they usually communicate their wishes and specify their conditions in writing.

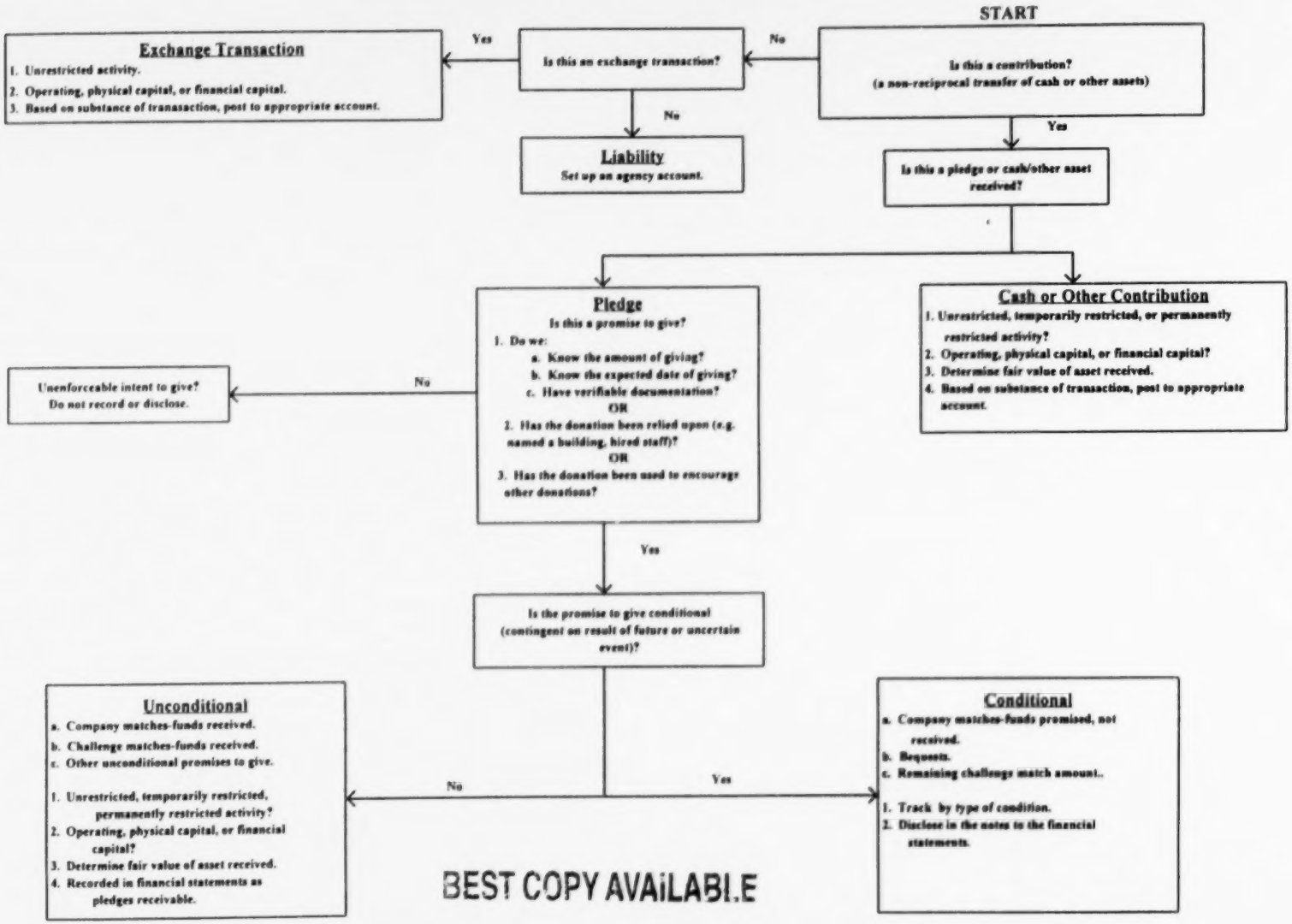
Pledge documents as a claim against an estate

Question: Some institutions have developed carefully worded pledge documents. Can these documents permit the institution to make a claim against the donor's estate?

Answer: Yes. Pledge documents can be constructed so that they could form the basis of a claim against a donor's estate, if necessary.

Figure 6

Identifying Promises to Give


START
Is this a contribution?
(a non-reciprocal transfer of cash or other assets)
No
Yes
Is this an exchange transaction?
Yes
No
Exchange Transaction
1. Unrestricted activity.
2. Operating, physical capital, or financial capital.
3. Based on substance of tranasaction, post to appropriate account.
Liability
Set up an agency account.
Is this a pledge or cash/other asset received?
Pledge
Is this a promise to give?
1. Do we:
a. Know the amount of giving?
b. Know the expected date of giving?
c. Have verifiable documentation?
OR
2. Has the donation been relied upon (e.g. named a building, hired staff)?
OR
3. Has the donation been used to encourage other donations?
Cash or Other Contribution
1. Unrestricted, temporarily restricted, or permanently restricted activity?
2. Operating, physical capital, or financial capital?
3. Determine fair value of asset received.
4. Based on subetance of transaction, post to appropriate account.
No
Unenforceable intent to give?
Do not record or disclose.
Yes
Is the promise to give conditional (contingent on result of future or uncertain event)?
No
Yes
Unconditional
a. Company matches-funds received.
b. Challenge matches-funds received.
c. Other unconditional promises to give.
1. Unrestricted, temporarily restricted, permanently restricted activity?
2. Operating, physical capital, or financial capital?
3. Determine fair value of asset received.
4. Recorded in financial statements as pledges receivable.
Conditional
a. Company matches-funds promised, not received.
b. Bequests.
c. Remaining challenge match amount..
1. Track by type of condition.
2. Disclose in the notes to the financial statements.

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C. Review Existing Systems

Building development systems

Question: In brief, are there three or four points that the development office should build into its systems to provide appropriate data to the finance office to comply with FASB Statement 116?

Answer: Yes, the following points should be built in:

- Amounts of unconditional promises
- Dates promises are expected to be received
- Specific purpose (if restricted for endowment, indicate whether the earned income is also restricted)
- Specific records for conditional promises, including the specific condition stipulated and the purpose if restricted

It is important to remember that complying with Statement No. 116 basically requires changes in year-end financial reporting. Conceivably, an institution could choose to leave all existing systems in place and only gather data at year-end sufficient to comply with the standard. For organizations with limited fund-raising, this may be an adequate approach. For others, the ongoing systems may be upgraded but issues such as collectibility of open pledges, aging of future promises, and distinguishing between conditional and unconditional promises may be addressed only at year-end. Finally, some institutions may use implementation of Statement 116 as rationalization for a major overhaul of their gift recording and reporting systems.

Changing development systems

Question: Will institutions need to make massive changes in their development information systems to accommodate FASB regulations?

Answer: In most cases, no. Assuming that all development offices are now keeping records on pledges, all that they will need to do is to formalize these records and make sure that due dates and restrictions are fully documented. However, an institution that routinely receives a considerable number of conditional promises would need to make more changes to its system. One institution determined that their existing gift recording system captured most of the necessary information. However, they decided to add a new field that would indicate whether the gift met Statement 116 requirements and therefore would be reported to the accounting office.

D. Compliance with Statement No. 116

Question: How do I begin to be sure our institution complies with the requirements of Statement No. 116?

Answer: Begin by reviewing your current policies and procedures concerning receipt and recording of gifts. How do existing development systems interrelate with the accounting system? What information is being captured in the existing systems, and will Statement 116 require more? One certainty is that closer ties between the development office and the business office will be necessary. Development staff will have to be familiar with the requirements of Statement 116, particularly as it pertains to appropriate documentation.

Someone within the organization has to have the responsibility for review of the documentation to determine whether a promise is recordable. The question has no single answer because so many variables exist. Most organizations probably capture much of the necessary information, although changes in systems may need to be made to improve reporting and facilitate the passing of data from the fund-raisers to the accountants.

Organizational involvement in the process

Question: Who needs to be involved in the process of reviewing and modifying existing policies and procedures?

Answer: Ultimately, Statement 116 changes financial and accounting reporting for gifts, pledges, collections, and contributed services, as well as reporting on the lifting of restrictions. Therefore the final responsibility should rest with the chief financial officer. At the same time, this will not be possible without the cooperation of the fund-raisers and development staff and those responsible for systems design and development. College or university counsel should be consulted for legal issues. In larger organizations, it may be appropriate to advise business managers of major units who may play a role in the receipt and recording of gifts.

E. Issues to Be Addressed

(i) Accrual Versus Cash

A decision will need to be made on accounting for contributions. Some will choose to record all transactions throughout the year on an accrual basis. Others will follow a cash basis throughout the year and adjust to accrual at year-end. Either is acceptable, and the decision will depend on the sophistication of existing systems.

III. Examples

Most of the following cases were developed by the staff of the Financial Accounting Standards Board for an instructional program on FASB Statement Nos. 116 and 117. In some cases, minor changes and additions have been made in some to fit them to the college and university environment. Not everyone will agree with the answers presented in these examples. They should be read as illustrative, rather than prescriptive. Suggested answers are provided at the end of the examples.

Example 1

University Hospital provides healthcare services to patients that are entitled to Medicaid assistance under a joint federal and state program. The program sets forth certain administrative and technical requirements covering provider participation, payment mechanisms, and individual eligibility and benefit provisions. Are the Medicaid payments received through the program contributions to University Hospital?

Example 2

WUTS, the university-owned public television station, conducts quarterly televised membership drives. With a membership fee of $50 or more, members receive a coffee mug (retail value $3.50); for over $75 , a tote bag (retail value $5); and for $300, a video tape of their choice (retail value $20). Are all of these items considered member fees contributions? How should WUTS account for the value of these items?

Example 3

As a fund raiser, the Music Department of Cultural College held a concert with a celebrity conducting the college's symphony orchestra. Tickets to all the activities sold for $200 and included a pre-performance cocktail party (fair value $25), admission to the concert (fair value $30), and a backstage reception following the performance (fair value $15). Are the tickets to the special event a contribution?

Example 4

Charitable Community College (CCC) receives $100,000 from Al Umnus under a charitable remainder trust agreement that designates CCC as the trustee and charitable remainder beneficiary. The terms of the trust require that CCC invest the assets and pay $5,000 each year to Mr. Umnus's son for the remainder of the son's life. Upon the death of the son, CCC may use its remainder interest for any purpose. Is the $100,000 a contribution?

Example 5

A state program provides money to private colleges and universities within the state that the institutions can use for any purpose. Each institution receives $250 per state resident enrolled full-time. All participating institutions must meet certain accreditation and nondiscrimination requirements and provide annual audited financial statements. Are the payments received by the institutions a contribution?

Example 6

Clean Air College receives $100,000 from Major Oil Corporation to research the effects of Major's new experimental gasoline additive on air pollution levels and engine condition. The college agrees to follow the protocol described by Major Oil in the award letter, complete the project promptly during the specified award period, and submit a project report and a financial report at the end of the project period. The college expects the project's direct costs to be about $75,000. Clean Air College agrees not to publish the results of the research for at least two years following the completion of the project; thereafter, any publication must contain a notice acknowledging Major Oil's support. Is the award a contribution?

Example 7

Best Cola (BC) enters into a $1 million agreement with Cardinal University (CU). CU agrees that for the next three years only Best Cola will be served in campus dining centers and in their sports facilities. CU also agrees to put BC's logo on the menu board in the dining halls and on the sports scoreboards. Is the agreement a contribution?

Example 8

Famous Foundation, which has a program to support musical performances, gives funds to the music department of Artistic College and specifies that the funds be used to support performing artists. As part of its regular program, the music department uses these funds to compensate individual artists who perform at the college and teach master classes. Is this a contribution?

Example 9

The women's soccer team at Good Sports College has been invited to participate in a tournament in England. The parents of the team members provide the funds to enable the team to go. Are these contributions?

Example 10

Amanda B. Rekonwith makes a $1 million gift to Siwash University and states that the income earned on its investment for the next 10 years is to support the women's studies program. At the end of that period, the university may use the fund, both principal and income, for whatever purpose it desires. How should this be recorded?

For examples 11 through 21, determine the following:

a. Is this contribution unrestricted, temporarily restricted, or permanently restricted?
b. Are there donor-imposed conditions?
c. Should the contribution be recognized currently, in the future, or not at all?
d. What is the amount of the contribution?

Example 11

The Food Maker Co. gave $500,000 to the college's Dietary Research Fund to commission a special study on the relationship between disease and high fat diets. The results of the study will be used to educate the public.

Example 12

David Diver will give the University $100,000 for its athletics program if he survives his next parachute jump off the Empire State Building scheduled for June 30.

Example 13

Outreach University has been offered the use of Thinkers Corporation conference facilities at the corporate headquarters for a series of special seminars scheduled off campus. The corporation stipulates that it must be reserved at least 30 days in advance and it will be approved if it is not being used for company business. Thinkers rents office space at $15 per square foot per year.

Example 14

The Creative College Art Museum sent out letters to its supporters asking for pledges as part of its "Purchase a Masterpiece" campaign. Genevieve Generous read the letter and sent in her response card with a pledge to contribute $500 in the next year.

Example 15

Sunny Skies gave 100 shares of Westwind Corporation to her alma mater, the College of Meteorology. The Westwind Corporation traded on the NYSE at a high of $16 and a low of $14 on the date of the gift.

Example 16

R.U. Ready gives $1 million to Serious University to support their program for students with learning disabilities. She specifies that the gift is to be invested and that the income is to be used to cover the costs of the program.

Example 17

Same example as 13, except Ms. Ready provides that the funds be held by the Tender Care Trust Company with the income to go in perpetuity to Serious University.

Example 18

The Classical Gas Company has agreed to contribute $100,000 in each of the next three years to support the concert series at Beethoven College. The college will acknowledge the company's contribution in the programs for the series.

Example 19

Research University receives an award notice of $500,000 from the NIH to research the effects of different diets on patients with heart problems. The NIH required a line-item budget. RU agrees to complete the project during the next two years, submit financial and project reports at the end of the project period, submit a copy of any articles published about the results of the research, and have the investigator discuss the project at an NIH seminar, if asked. RU further

agrees to draw upon a letter of credit to cover disbursements and return any unspent funds at the end of the project period.

Example 20

Clarissa Charitable donated her home next to the campus for use as a faculty residence. The cost to Ms. Charitable was $55,000. The home was appraised by one professional real estate appraiser for $100,000 and by another for $110,000.

Example 21

Hiram History has an audiotape collection, an oral history project, that he wants to give to the Old University Library. The tapes are recordings of many people who were connected with OU from the time of its founding.

For examples 22 through 28, determine the following:

a. Are the items conditional or unconditional?
b. Should the items be recognized currently, in the future, or not at all?
c. Are the items unrestricted, temporarily restricted, or permanently restricted?
d. What is the amount that will be recognized in the financial statements as a contribution?

Example 22

The Office Machine Co. has a corporate giving program that promises to contribute $100,000 of office equipment within the fiscal year to Technical School of Technology. The equipment will be used in the school's administrative offices.

Example 23

I. M. Wealthy notifies Needy College that he plans to give $1 million over the next several years to support the Wealthy Chair for the Study of Free Enterprise. The funds will come from 10 percent of his company's after-tax profits, which he estimates would be about $200,000 annually. In the event that the gift is not completed by the time of his death, Mr. Wealthy's will provides for completing the pledge.

Example 24

Ima Starr, an alumnus of Performing Arts College, has notified the college that she will donate to the college any net proceeds in excess of $25,000 from her next concert. She states that the funds are to be used to improve the seating and lighting in the college's theater.

Example 25

The Hal Lowed Foundation has awarded $2 million to ABC University that will be paid prior to the year end for an undergraduate financial aid fund. The Lowed Foundation wants the gift to be invested in perpetuity and the earnings on the fund to be used for student aid.

Example 26

I. M. Generous answered a pledge card from the Olympic College athletic department promising to give $5,000 over a four-year period to support women's sports.

Example 27

The University Hospital was recently served with a malpractice lawsuit. Boris Barrister, the chancellor's brother-in-law and a renowned trial attorney, decided to assist in the defense of the hospital. Usually, Mr. Barrister works for a fee of $400 an hour plus expenses. For this case, Barrister charged only his expenses.

Example 28

Deborah Debit, a CPA, spent Sunday afternoon at the college's art museum sending out a mailing to Friends of the Museum seeking contributions to the building fund.

Example 29

To do her part, Ms. Debit said she also plans to contribute $5,000.

Answers to Examples

Example 1

Medicaid payments made to the University Hospital are not contributions; they are third-party payments for services rendered. The University Hospital provides patient care services for a fee—an exchange transaction—and acts as an intermediary between the government providers and the eligible beneficiaries.

Example 2

The member fees are contributions. The token items offered have nominal value. WUTS would account for the cost of the items as fund-raising expense. Alternatively, WUTS may consider this to be two separate transactions—the sale of the token item at its retail value and contribution of the excess of the membership fee over the sale's price of the token item. The cost of the token item would be included in the cost of goods sold.

Example 3

The excess of the ticket price over the fair value of the benefits received by the donors ($130) is a contribution.

Example 4

The transfer is partially an exchange, an agreement for annuity payments to a beneficiary over a specified time, and partially a contribution. The contribution received by CCC is the unconditional right to receive the remainder interest of the annuity trust. The amount of the contribution is the fair value of the assets transferred ($100,000) less the fair value of the estimated annuity payments—the present value of $5,000 a year to be paid to annually over the expected life of Mr. Umnus's son.

Example 5

The payments received are a contribution. They are voluntary and nonreciprocal and support a public purpose, rather than providing benefits directly to the state. The fact that aid is being allocated by a formula does not make the contribution reciprocal.

Some may argue that the transaction is reciprocal because the state has a fundamental responsibility to educate its citizens and that it "hires" the institutions to fulfill that responsibility. However, the amount of the contribution is insignificant in relation to the cost of educating the student.

In contrast, some states that don't have veterinary colleges "buy" spaces for their residents in veterinary colleges in other states. The payments are usually greater than tuition costs at those colleges. These would be an exchange transaction and not a gift.

Example 6

The award is an exchange transaction. The research is directly related to Major Oil's business activities. If successful, the additive will have significant benefits to the company. Major Oil has specified how the testing is to be done and has retained exclusive rights to the research rights for two years, which may be adequate for it to obtain a competitive market advantage. The difference between the estimated costs and the total award are a reasonable estimate of the indirect costs associated with the project.

Example 7

The privileges given to BC are more than mere acknowledgments of a contribution. The answer to this example depends on the value assigned to the exclusive access given. The transaction is either an exchange or part exchange and part contribution. CU should determine the fair value of the exclusivity arrangement and of the advertising. CU might request an appraisal of the contract from a marketing consultant. If $1 million is not a reasonable estimate of the fair value of the rights and advertising, the excess of $1 million over that fair value would be a contribution.

Example 8

Yes. The college is not acting as an intermediary for these artists. The funds are in support of an on-going program and should be recognized as a contribution.

Example 9

Yes. The parents are making a contribution to an organized activity of the college and the college is the sponsor of the activity.

Example 10

This is a term endowment. It should be recognized as an addition to temporarily restricted net assets for a restricted purpose. At the end of the 10-year period, it should be reclassified to unrestricted net assets.

Example 11

This is a contribution. The results are to benefit the public, not the company.

a. The contribution is temporarily restricted as to purpose.
b. There are no donor-imposed restrictions; the contribution is unconditional.
c. The contribution should be recognized currently.
d. The amount of the contribution is $500,000.

Example 12

This is a promised contribution.

a. The contribution is temporarily restricted as to purpose and as to time.
b. The contribution is conditional upon Diver's survival.

c. If he survives his jump, the contribution should be recognized on June 30.
d. The amount of the contribution is $100,000.

Example 13

This is a contributed use of facilities.

a. The contribution is unrestricted.
b. The contribution is conditional upon reservation, approval, and availability.
c. The contribution should be recognized at the time the space is utilized because at that time all conditions are satisfied.
d. The amount of the contribution should be calculated at a rate somewhat less than the $15 per square foot for space used. The discount from the full rate is to reflect the limitations placed on the reservation of the space.

Example 14

This illustrates a restriction implied from the circumstances surrounding the solicitation.

a. The contribution is temporarily restricted.
b. The contribution is unconditional.
c. The contribution should be recognized currently.
d. The amount of the contribution is $500.

Example 15

a. The contribution is unrestricted.
b. The contribution is unconditional.
c. The contribution should be recognized currently.
d. The amount of the contribution is $1,500; recognized at fair market value or the average price for the day.

Example 16

a. The contribution is permanently restricted as to contribution, temporarily restricted as to income.
b. The contribution is unconditional.
c. The gift should be recognized currently; the income when earned.
d. The amount of the contribution is $1 million.

Example 17

Same answers as 13. The assumption is that the present value of the future income streams in perpetuity is equal to the current value of the gift.

Example 18

This example illustrates that a mere acknowledgment does not create an exchange situation.

a. The contribution is temporarily restricted as to purpose and as to time.
b. The contribution is unconditional.
c. The contribution should be recognized currently.
d. The amount of the contribution is $100,000 for the first year plus the second and third years' contributions appropriately discounted.

Example 19

This is an example of a grant that is a contribution. If the NIH is using the results of the research for its own benefit, the transaction may be an exchange.

a. The contribution is temporarily restricted as to purpose.
b. The contribution is conditioned as to the amount of funds spent.
c. The contribution should be recognized equal to cash expenditure.
d. The amount of the contribution is the amount of funds spent, up to maximum of $500,000.

Example 20

a. The contribution is either unrestricted or temporarily restricted, dependent on the policy decision of the organization. An organization is permitted to adopt a policy of implying a time restriction that expires over the life of the asset.
b. The contribution is unconditional.
c. The contribution should be recognized currently.
d. The contribution amount should be determined using a fair market value estimate, such as the average of the two appraisals.

Example 21

This illustrates a collection item with a value that is either uncertain or perhaps zero.

a. The contribution is unrestricted.
b. The contribution is unconditional.
c. The contribution should not be recognized.
d. The amount of the contribution is zero. The item is saved only for its potential future use in educational research and has no known alternative use.

Example 22

This example is a promise to give.

a. The contribution is unconditional.
b. The contribution is recognized currently.
c. The contribution is unrestricted or temporarily restricted.
d. The amount of the contribution is $100,000.

Example 23

This is an intention to give. Neither the gift from receipts nor the provision in Mr. Wealthy's will is a promise.

a. The item is conditional.
b. The item should be recognized in the future.
c. The item is temporarily restricted as to purpose.
d. The contribution amount is the amount of cash received.

Example 24

This is a promise to give.

a. This is a conditional contribution: at least $25,000 must be earned before the college gets any money.
b. The amount should be recognized when the condition is met.
c. The item is temporarily restricted as to purpose.
d. The amount of concert proceeds in excess of $25,000 should be recognized as a contribution.

Example 25

This is a promise to give.

a. The contribution is unconditional.
b. The item should be recognized currently.
c. The contribution is permanently restricted for $2 million, and income is temporarily restricted.
d. The $2 million should be recognized now; the income when earned.

Example 26

This is a promise to give.

a. The contribution is unconditional.
b. The contribution should be recognized currently.
c. The contribution is temporarily restricted by time.
d. The amount that should be recognized as a contribution is the present value of the $5,000 over four years at an interest rate commensurate with the risks involved.

Example 27

This item falls under contributed services.

a. The contribution is unconditional.
b. The contribution should be recognized currently.
c. The contribution is unrestricted.
d. The fair value of Barrister's services at a rate of $400 per hour should be recognized as a contribution.

Example 28

This is a contributed service that does not meet the criterion of requiring specialized skills. Do not recognize.

Example 29

This is the communication of a plan of intention rather than promise to give.

a. The contribution is unconditional.
b. The contribution is not a promise and should not be recognized.
c. The item is temporarily restricted for the building fund.
d. The amount that should be recognized as a contribution is zero.

Glossary of Terms from FASB Statement No. 116

Collections: Works of art, historical treasures, or similar assets that are (a) held for public exhibition, education, or research in furtherance of public service rather than financial gain; (b) protected, kept unencumbered, cared for, and preserved; and (c) subject to an organizational policy that requires the proceeds of items that are sold to be used to acquire other items for collections.

Conditional Promise to Give: A promise to give that depends on the occurrence of a specified future and uncertain event to bind the promisor.

Contribution: An unconditional transfer of cash or other assets to an entity or a settlement or cancellation of its liabilities in a voluntary transfer by another entity acting other than as an owner.

Donor-Imposed Condition: A donor stipulation that specifies a future and uncertain event whose occurrence or failure to occur gives the promisor a right of return of the assets it has transferred or releases the promisor from its obligation to transfer its assets.

Donor-Imposed Restriction: A donor stipulation that specifies a use for the contributed asset that is more specific than broad limits resulting from the nature of the organization, the environment in which it operates, and the purposes specified in its articles of incorporation or bylaws or comparable documents for an unincorporated association. A restriction on an organization's use of the assets contributed may be temporary or permanent.

Nonreciprocal Transfer: A transaction in which an entity incurs a liability or transfers an asset to another entity (or receives an asset or cancellation of a liability) without directly receiving (or giving) value in exchange.

Permanent Restriction: A donor-imposed restriction that stipulates that resources be maintained permanently but permits the organization to use up or expend part or all of the income (or other economic benefit) derived from the donated assets.

Permanently Restricted Net Assets: The part of the net assets of a nonprofit organization resulting (a) from contributions and other inflows of assets whose use by the organization is limited by donor-imposed stipulations that neither expire by passage of time nor can be fulfilled or otherwise removed by actions of the organization; (b) from other asset enhancements and diminishments subject to the same kinds of stipulations; and (c) from reclassifications from (or to) other classes of net assets as a consequence of donor-imposed stipulations.

Promise to Give: A written or oral agreement to contribute cash or other assets to another entity. A promise to give may be either conditional or unconditional.

Restricted Support: Donor-restricted revenues or gains from contributions that increase either temporarily restricted net assets or permanently restricted net assets.

Temporarily Restricted Net Assets: The part of the net assets of a nonprofit organization resulting (a) from contributions and other inflows of assets whose use by the organization is limited by donor-imposed stipulations that either expire by passage of time or can be fulfilled and removed by actions of the organization pursuant to those stipulations; (b) from other asset enhancements and diminishments subject to the same kinds of stipulations; and (c) from reclassifications to (or from) other classes of net assets as a consequence of donor-imposed stipulations, their expiration by passage of time, or their fulfillment and removal by actions of the organization pursuant to the stipulations.

Temporary Restrictions: A donor-imposed restriction that permits the donee organization to use up or expend the donated assets as specified and is satisfied by the passage of time or by actions of the organization.

Unconditional Promise to Give: A promise to give that depends only on the passage of time or demand by the promisee for performance.

Unrestricted Net Assets: The part of the net assets of a nonprofit organization that is neither permanently restricted nor temporarily restricted by donor-imposed stipulations.

Unrestricted Support: Revenues or gains from contributions that are not restricted by donors.

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